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GOVERNMENT CHECK CASHING, "LIFELINE" CHECKING, AND THE COMMUNITY REINVESTMENT ACT

HEARINGS

BEFORE THE

SUBCOMMITTEE ON
CONSUMER AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

S. 906

TO PROVIDE ACCESS TO CHECK CASHING SERVICES

S. 907

TO PROVIDE ACCESS TO BASIC BANKING SERVICES

S. 909

TO AMEND THE COMMUNITY REINVESTMENT ACT OF 1977 TO REQUIRE WRITTEN EVALUATIONS

JUNE 6 AND 7, 1989

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

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CONTENTS

TUESDAY, JUNE 6, 1989

Page
Opening statement of Senator Dixon 1
Opening statement of Senator D'Amato 39
Opening statement of Senator Kerry 40
Opening remarks of Senator Bond 69
Opening remarks of Senator Specter 83
Text of the bills:
  S. 906 8
  S. 907 21
  S. 909 36

WITNESSES

Howard M. Metzenbaum, U.S. Senator from the State of Ohio 2
  Prepared statement 6
Howard B. Brown, Banking Commissioner, State of Connecticut 41
  Public Act 87-24 41
  Background of the law 42
  Prepared statement 45
  Response to written questions of Senator Dixon 306
William E. Douglas, Commissioner, The Financial Management Service, Department of the Treasury 49
  Prepared statement 51
  Response to written questions of Senator Dixon 314
Jerome S. Gagerman, president, National Check Cashers Association 55
  Code of conduct 55
  Alternate means of benefit distribution 57
  Prepared statement 58
  Response to written questions of Senator Dixon 323
Rosemary Dunlap, Virginia Citizens Consumer Council 63
  Prepared statement 66
    Background 66
    Survey 66
    Results 66
    Payroll check 66
    Government checks 66
    Personal checks 66
    Other fees 67
    Money orders 67
    Outlets refusing to give information 67
    Differences within cities 67
    Total annual costs 67
    Regulation of check cashing services 67
    Recommendations 67
Panel discussion:
  Profit for cashing checks 70
  Fraud and forgery 70
  Direct deposit 72
  Insurance against loss 72
  Foes of direct deposit 74
  Solving the problem without Federal legislation 76
  Check cashers are convenient 78
  Fees changed over 81

Page

- Robert L. Stevens, president, Bryn Mawr Trust Co.; on behalf of The American Bankers Association ... 84
  - Prepared statement ... 97
    - Introduction ... 88
    - Basic banking and government check cashing ... 90
    - Community Reinvestment Act ... 97
    - Conclusion ... 101
    - Appendix ... 103
  - Response to written questions of Senator Dixon ... 332
- Richard A. Loundy, chairman of the board, Devon Bank, Chicago, IL; representing The Independent Bankers Association of America ... 105
  - Prepared statement ... 108
    - Government check cashing ... 108
    - Basic banking accounts ... 109
    - Community Reinvestment Act ... 110
    - Conclusion ... 6
  - Response to written questions of Senator Dixon ... 345
- John P. Kelly, president, National Bankers Association ... 124
  - Prepared statement ... 127
    - Introduction ... 127
    - Background ... 127
    - Basic banking services ... 127
    - Government check cashing ... 128
    - Community Reinvestment Act ... 129
    - Alternate approaches ... 130
    - Electronic Benefit Services Program ... 130
    - Conclusion ... 131
  - Response to written questions of Senator Dixon ... 349
- Robert J. Sell, member, National Legislative Council, American Association of Retired Persons ... 132
  - Prepared statement ... 134
    - Introducion ... 134
    - Basic banking accounts ... 134
    - Government check cashing ... 135
    - AARP opposition to mandated direct deposit ... 135
    - Conclusion ... 136
  - Response to written questions of Senator Dixon ... 351
- Peggy Miller, legislative representative, Consumer Federation of America, Washington, DC ... 137
  - Prepared statement ... 140
    - Background/problem ... 140
    - Check cashing ... 142
    - Problems of fraud ... 142
    - Lifeline banking ... 143
    - Community Reinvestment Act ... 144
  - Response to written questions of Senator Dixon ... 353

Panel discussion:

- Check cashing ... 146
- Competing with banks ... 148
- Concerns about fraud ... 150
- Direct deposit ... 151
- Profit from float time on checks ... 153

WEDNESDAY, JUNE 7, 1989

- Opening statement of Senator Dixon ... 159
- Opening remarks of Senator Bond ... 174
- Opening statement of Chairman Riegle ... 204
- Opening statement of Senator D'Amato ... 231

WITNESSES

- Martha R. Seger, member, Board of Governors, Federal Reserve System ... 160
  - Prepared statement ... 163
    - Summary ... 163
    - S. 909 ... 167

Martha R. Seger, member, Board of Governors, Federal Reserve System—Continued
  Prepared statement—Continued

Page

    CRA amendment to H.R. 176 ... 169
  Response to written questions of Senator Dixon ... 356

Witness discussion:

  The rating system ... 176
  How ratings are determined ... 178
  CRA challenges ... 179
Ted Wysocki, executive director, Chicago Association of Neighborhood Development Organizations ... 185
  Investment in neighborhood development ... 186
  Suggestions to improve CRA exams ... 187
  Prepared statement ... 188
Marion R. Foote, senior vice president/department head, specialized financial services, First Chicago Corp ... 195
  Prepared statement ... 198
    Responsible leadership ... 199
    Sound business principles ... 200
    Availability of Federal resources ... 201
    Multifaceted approach ... 201
    Availability of skilled entrepreneurs ... 202
Charles F. Clement, senior vice president, Landmark Bank, St. Louis, MO ... 205
  Discounted loans ... 206
  Prepared statement ... 208
Mary Ann Cunningham, representing the Association of Community Organizations for Reform Now ... 210
  Prepared statement ... 212
    ACORN ... 212
    CRA exam disclosure ... 213
    Successes in St. Louis ... 214
Charles H. Grice, managing director, Community Reinvestment Institute, San Francisco, CA ... 232
  Prepared statement ... 235
    Community Reinvestment Institute ... 235
    Improving the Community Reinvestment Act ... 235
    CRA successes are there ... 235
    Fear and confusion remain ... 236
    How Congress can help ... 236
    Let the new regulatory regime take effect ... 236
    Oversight ... 236
    Help provide more tools ... 236
    The focus belongs on the examination process ... 237
    Increase public disclosures ... 238
  Response to written questions of Senator Dixon ... 360

Panel discussion:

  Community Reinvestment Institute ... 239
  Creative use of State funds ... 241
  Community participation ... 243
  Financial institutions obligations ... 244
Jonathan Brown, director, BankWatch, Washington, DC ... 246
Allen J. Fishbein, general counsel, Center for Community Change, Washington, DC ... 249
  Prepared statement of Messrs. Brown and Fishbein ... 252
    Summary ... 252
    Introduction ... 253
    CRA agreements can make a difference ... 253
    Last year's CRA oversight hearings demonstrate the need for reform . 254
    Recent developments raise new issues about the adequacy of agency enforcement ... 254
    The procedural rights of citizens in the application review process must be perserved ... 255
    Comments on legislative proposals before the subcommittee ... 255
John M. Kolesar, president, AmeriTrust Development Bank, Cleveland, OH; representing the Consumer Bankers Association ... 257
  Prepared statement ... 260

John M. Kolesar, president, AmeriTrust Development Bank, Cleveland, OH; representing the Consumer Bankers Association—Continued
  Prepared statement—Continued
    I. The procedural inequities and bias experienced by financial institutions under CRA ..... Page 260
    II. Recent developments do not redress the existing inequities 261
    III. Possible CRA refinements 262
    Conclusion 265
  Response to written questions of Senator Dixon 362
Charles G. Conville, president and CEO, PrimeBank, Federal Savings Bank, Grand Rapids, MI; treasurer, National Council of Savings Institutions 266
  Prepared statement 268
    Community Reinvestment Act 268
    S. 909 269
    CRA amendment to H.R. 176 270
    S. 906 270
    S. 907 271
    Relationship with State law 271
Panel discussion:
  Positive incentives 281
  Community groups may file a challenge 300
  Agency enforcement 302

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Statements:
  National Association of Federal Credit Unions 367
  Electronic Funds Transfer Association 370
  Consumer Bankers Association 374
Report from the U.S. General Accounting Office entitled, "Banking—Government Check-Cashing Issues," October 1988 383

GOVERNMENT CHECK CASHING, "LIFELINE" CHECKING, AND THE COMMUNITY REINVESTMENT ACT

TUESDAY, JUNE 6, 1989

U.S. Senate,
Committee on Banking, Housing, and Urban Affairs,
Subcommittee on Consumer and Regulatory Affairs,
Washington, DC.

The subcommittee met at 9 a.m., in room SD–538, Dirksen Senate Office Building, Senator Alan J. Dixon (chairman of the subcommittee) presiding.

Present: Senators Dixon, Dodd, Kerry, Bryan, D'Amato, Bond, Specter, and Metzenbaum.

OPENING STATEMENT OF SENATOR DIXON

Senator Dixon. Ladies and gentlemen, this subcommittee meeting of the Consumer and Regulatory Affairs Subcommittee of the Banking Committee will come to order.

Back in April, I promised my good friend, Senator Howard Metzenbaum, to hold hearings on four consumer issues. This morning we begin 2 days of hearings on three of those issues. Today, our hearing focuses on Government check cashing and lifeline checking, and tomorrow we will cover the Community Reinvestment Act, especially the public disclosure issue.

The fourth matter, discrimination in home mortgages and commercial lending we will deal with in a separate hearing probably in September. That hearing will fulfill my commitment to my colleague from Ohio, but I want to say this, Howard. I was planning to have that hearing anyway, but we are delighted to have you here. We put a section in the FSLIC bill requiring reports on this matter by the various regulators within 60 days and this subcommittee will hold a hearing once those reports are ready. We will not tolerate continuing discrimination or redlining. It's illegal and it has to stop.

Today, however, we will explore other issues—how people, particularly low-income people, cash their government checks; whether they use depository institutions; how much they have to pay to cash a check or keep a simple bank account. Unlike discrimination in lending, there are no Federal laws on these subjects.

The question before us, of course, is whether there ought to be. Senator Metzenbaum believes there should be, and we will consider his bills, S. 906 and 907 today. We will consider whether or not these two bills offer the best solution or whether other measures are needed and whether legislation is the best answer.

Frankly, I have no fixed conclusion on these questions. I intend to listen carefully to our witnesses' testimony—as you know, I always listen carefully to Chicagoans and I welcome the fact that there are three here, Jerry Gagerman, Richard Loundy, and Robert Sell. Illinois is representative of America we think, Howard, and the witnesses today from Illinois represent every perspective on these issues. But I want to put all the witnesses on notice, whether or not you're from my home State. I intend to listen carefully and ask you the critical questions.

Last time the Banking Committee held hearings on these issues the GAO had not yet completed its report. Since then it has, and I've reviewed the results. Two figures I think stand out. First, 17 percent of our people do not have any sort of banking account at all. I ask, has that figure been increasing and would legislation change it? Second, only 18 percent of banks offer to the general public we are told a low-cost, low-minimum balance, basic bank account. Is there more demand for this account? One would presume so, but I want facts not just presumptions.

There is more demand by our senior citizens and, again according to the GAO, 76 percent of banks do offer some sort of discounted account to senior citizens.

I hope today and tomorrow that all of us will listen to one another, rather than talk past each other; that we will focus on real problems, rather than our own set agendas; and that we will venture to think creatively, rather than merely defend our preconceptions; that we will focus on an objective and then figure out realistically how best to meet it.

Now, ladies and gentlemen, there are going to be some time problems unless we have time constraints. With the exception of my colleague who is a sponsor of this legislation, the distinguished Senator from Ohio, I would ask other witnesses to complete their remarks within 7 minutes. The entire statement you have will be placed in the record. I would greatly appreciate it if you would limit your remarks to 7 minutes. That will not apply, may I say, to my colleague from Ohio and we are delighted to welcome him to this subcommittee this morning. He is a man of great note from the standpoint of his brevity in any event.

STATEMENT OF HOWARD M. METZENBAUM, U.S. SENATOR FROM THE STATE OF OHIO

Senator METZENBAUM. Mr. Chairman, I am very happy to be here and, as you know, I have not been reluctant to speak at length on the floor of the Senate or to take the time of the Senate if I thought the issue is of that kind of importance. I will not follow that procedure today. I will be brief because I very much appreciate the fact that the chairman has promised me that he would hold hearings on these important consumer issues and very promptly followed through. I know that the chairman is a man of his word and the chairman is certainly unquestionably one of the most respected members of the U.S. Senate and I consider it a privilege to have the opportunity to work with him here this morning as well as on the floor every day of the week.

The hearings today involve three separate issues—the government check cashing matter, the basic lifeline account, and community reinvestment.

Frankly, Mr. Chairman, these are not new issues. They have a long history and I would hope that the history might be concluded during this session of the Congress because it's becoming wearisome every time there's a banking bill or savings and loan bill or anything similar thereto to go to the floor and offer an amendment on these subjects which I have done in the past and which I hope I won't have to do in the future.

In the past, when these issues came up, when Senator Proxmire was the chairman, he asked me to hold up while there be hearings in the committee. I did that. This time Senator Riegle and you asked me to hold up while there be hearings in the committee and I'm happy to accommodate.

Frankly, these proposals have made it to various stages of the legislative process. They haven't died just aborning. In fact, an amendment I offered to provide for free government check cashing passed the Senate 2 years ago and last year the Banking Committee agreed to include a government check cashing proposal in its final version of the bill expanding the powers of banks. Unfortunately, that bill never made it to the floor.

Government check cashing, lifeline banking, and community reinvestment, have followed a similar course in the House.

The fact is, these proposals are still not law and the banking needs of low and moderate income Americans are still being ignored. I hope that we can dispose of these issues once and for all.

Frankly, Mr. Chairman, I have attempted and gone out of my way to send out as many messages as I know to the banking institutions and the financial institutions involved and said, "Let us work together." And they have not been willing to work together. I think my staff submitted to your staff a comparison with my original legislation on check cashing and the compromises that have been made. But still, we don't have the banks on board with us.

So it seems to me that those financial institutions that continue to fight these modest proposals have to once and for all come forward and say, "We'll agree to this, that or something else," or we have to take the position that we are going to pass it with or without their concurrence.

Frankly, banks and financial institutions have no problem asking for special treatment for themselves. One could orchestrate a beautiful sonata on the basis of all of the legislative proposals that we constantly deal with having to do with financial institutions and what financial institutions want.

Banks want Congress to enact sweeping legislation to allow them into lucrative insurance and securities fields. Savings and loans want Congress to rescue them from a financial crisis which is in large part of their own making—this rescue will cost $239 billion, according to Senator Riegle's figure on the floor of the Senate. And taxpayers are going to wind up paying a large part of the tab.

But when the banks or the savings and loans are asked to do something that is people-oriented, oh, no, that will destroy the institution. These banks and savings and loan institutions refuse to give something back to the American people.

When they ask us for help, that's great. When we tell them what we think they ought to do in order to help people in some modest way, they shout, "Government interference."

Let's tell the banks and savings and loans that it's time they cashed Social Security and other government checks for noncustomers. Who has these government checks? These are the poor. These are the aged. These are the veterans. These are the people who don't have the extra dollars available to pay the check cashing costs.

Frankly, it's time that the banks and savings and loans offer low-cost bank accounts to families struggling to make ends meet. It's time they let the public know about their investments in the neighborhoods in which they operate.

Now I have three bills which will accomplish these objectives. S. 906 would require financial institutions to cash government checks for non-customers for a small fee. S. 907 would require these institutions to offer low-cost lifeline banking accounts. S. 909 would require the disclosure of financial institutions' community reinvestment evaluations and ratings.

These are modest proposals. This is not drastic or draconian legislation. They are very modest proposals.

Today, individuals trying to cash government-issued checks are being turned away from neighborhood banks because they don't hold accounts in those banks. Many of these same individuals are paying $5, $10 and $25 to cash $500 government assistance checks.

I've been to some areas of the country where you see the most beautiful new buildings built by these check-cashing operations.

They are built on the sweat and toil and hard-earned dollars of poor people who have no other place to turn to get their check cashed. And these check-cashing institutions—and I don't fault them—they are performing a service. I'm not saying that they are ogres and I have some negative feeling about them. But frankly, government check cashing is a service that ought to be covered by the banks and the other financial institutions in our economy.

Right now as many as one in five families—this conforms with the figures that the chairman just mentioned—one in five families has no relationship with a bank. I think he used 17 percent or 18 percent. Many more families are being driven away from banking because they can't afford the maintenance fees. And currently some financial institutions are continuing to ignore the Community Reinvestment Act of 1977 and its dictate to invest in neighborhood communities. We've got to put a stop to this.

The bills I've offered this year will help make banks and savings and loans more responsive to the needs of low and middle income Americans. They are reasonable proposals. I'm willing to listen to any suggestions for improving the bills, but we must put an end to the delays once and for all.

I have said time and time again, let us work together with the financial institutions. I don't want to put any undue burden or oppressive burden on them. But I believe that they have a community responsibility. I think they have a responsibility to those who receive government checks and I'm hopeful that this committee will see fit to promptly move forward with legislation that will achieve the three objectives that are covered in the three pieces of legislation that are before you.

Frankly, Mr. Chairman, I'm tired of going to the floor with amendments. I would hope that this committee will come forward with legislation so that the Senate and the House will once and for all have an opportunity to pass upon these bills in an up or down vote.

Mr. Chairman, I thank you for your consideration.

[The complete prepared statement of Senator Metzenbaum and copies of the proposed bills follow:]

PREPARED STATEMENT OF SENATOR METZENBAUM

I APPRECIATE THE CHAIRMAN HOLDING TWO DAYS OF HEARINGS ON THREE VERY IMPORTANT CONSUMER BANKING ISSUES: GOVERNMENT CHECK CASHING, BASIC "LIFELINE" BANKING ACCOUNTS AND COMMUNITY REINVESTMENT.

THESE ARE NOT NEW ISSUES. INDEED, THEY HAVE A LONG HISTORY.

THEY'VE BEEN THE SUBJECT OF SEVERAL HEARINGS.

THEY'VE MADE IT TO VARIOUS STAGES OF THE LEGISLATIVE PROCESS.

IN FACT, AN AMENDMENT I OFFERED TO PROVIDE FOR FREE GOVERNMENT CHECK CASHING PASSED THE SENATE TWO YEARS AGO. AND, LAST YEAR, THE BANKING COMMITTEE AGREED TO INCLUDE A GOVERNMENT CHECK CASHING PROPOSAL IN ITS FINAL VERSION OF THE BILL EXPANDING THE POWERS OF BANKS.

THAT BILL NEVER MADE IT TO THE FLOOR.

GOVERNMENT CHECK CASHING, "LIFELINE" BANKING, AND COMMUNITY REINVESTMENT HAVE FOLLOWED A SIMILAR COURSE IN THE HOUSE.

THEY STILL ARE NOT LAW. AS A RESULT, THE BANKING NEEDS OF LOW AND MODERATE INCOME AMERICANS ARE STILL BEING IGNORED.

LET'S DISPOSE OF THESE ISSUES ONCE AND FOR ALL.

I'VE HAD IT WITH THOSE FINANCIAL INSTITUTIONS THAT CONTINUE TO FIGHT THESE MODEST PROPOSALS.

THEY HAVE NO PROBLEM ASKING FOR SPECIAL TREATMENT FOR THEMSELVES.

BANKS WANT CONGRESS TO ENACT SWEEPING LEGISLATION TO ALLOW THEM INTO LUCRATIVE INSURANCE AND SECURITIES FIELDS.

SAVINGS AND LOANS WANT CONGRESS TO RESCUE THEM FROM A FINANCIAL CRISIS WHICH IS IN LARGE PART OF THEIR OWN MAKING. TAXPAYERS ARE GOING TO WIND UP SPENDING BILLIONS OF DOLLARS FOR THAT PRIVILEGE.

YET THESE SAME BANKS AND SAVINGS AND LOANS REFUSE TO GIVE SOMETHING BACK TO THE AMERICAN PEOPLE. THAT'S WHEN THEY SHOUT "GOVERNMENT INTERFERENCE."

LET'S TELL THE BANKS AND SAVINGS AND LOANS THAT IT'S TIME THEY CASHED SOCIAL SECURITY AND OTHER GOVERNMENT CHECKS FOR NON-CUSTOMERS. IT'S TIME THEY OFFERED LOW-COST BANK ACCOUNTS TO FAMILIES STRUGGLING TO MAKE ENDS MEET. AND IT'S TIME THEY LET THE PUBLIC KNOW ABOUT THEIR INVESTMENTS IN THE NEIGHBORHOODS IN WHICH THEY OPERATE.

I HAVE THREE BILLS WHICH WILL ACCOMPLISH THESE OBJECTIVES.

S. 906 WOULD REQUIRE FINANCIAL INSTITUTIONS TO CASH GOVERNMENT CHECKS FOR NON-CUSTOMERS FOR A SMALL FEE.

S. 907 WOULD REQUIRE THESE INSTITUTIONS TO OFFER LOW COST "LIFELINE" BANKING ACCOUNTS.

S. 909 WOULD REQUIRE THE DISCLOSURE OF FINANCIAL INSTITUTIONS' COMMUNITY REINVESTMENT EVALUATIONS AND RATINGS.

THEY ARE MODEST PROPOSALS. BUT THEY ARE VERY IMPORTANT.

TODAY, INDIVIDUALS, TRYING TO CASH GOVERNMENT ISSUED CHECKS, ARE BEING TURNED AWAY FROM NEIGHBORHOOD BANKS BECAUSE THEY DON'T HOLD ACCOUNTS IN THOSE BANKS. MANY OF THESE SAME INDIVIDUALS ARE PAYING $5, $10 & $25 TO CASH $500 GOVERNMENT ASSISTANCE CHECKS.

RIGHT NOW, AS MANY AS 1 IN 5 FAMILIES HAS NO RELATIONSHIP WITH A BANK. MANY MORE FAMILIES ARE BEING DRIVEN AWAY FROM THE BANKING SYSTEM BECAUSE THEY CAN'T AFFORD THE MAINTENANCE FEES.

AND, CURRENTLY, SOME FINANCIAL INSTITUTIONS ARE CONTINUING TO IGNORE THE COMMUNITY REINVESTMENT ACT OF 1977 AND IT'S DICTATE TO INVEST IN NEIGHBORHOOD COMMUNITIES.

WE'VE GOT TO STOP THIS.

THE BILLS I HAVE OFFERED THIS YEAR WILL HELP MAKE BANKS AND SAVINGS AND LOANS MORE RESPONSIVE TO THE NEEDS OF LOW AND MIDDLE INCOME AMERICANS. THEY ARE REASONABLE PROPOSALS. HOWEVER, I AM WILLING TO LISTEN TO ANY SUGGESTIONS FOR IMPROVING THEM. BUT WE SIMPLY MUST PUT AN END TO THE DELAYS ONCE AND FOR ALL. I URGE THE CHAIRMAN AND OTHER MEMBERS OF THIS SUBCOMMITTEE TO HELP ENACT THESE IMPORTANT BILLS.

II

101st CONGRESS
1st Session

S. 906

To provide access to check cashing services.

IN THE SENATE OF THE UNITED STATES

May 3 (legislative day, January 3), 1989

Mr. Metzenbaum introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

A BILL

To provide access to check cashing services.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Government Check Cashing Act of 1989.".

SEC. 2. GOVERNMENT CHECK CASHING SERVICES.

(a) Requirement to Offer Services.—Each depository institution shall offer a government check cashing service that meets the requirements of this section.

(b) Terms and Conditions of Service.—A government check cashing service offered by a depository institution meets the requirements of this section if it is a service—

(1) which is available to individuals (or to members, in the case of a credit union) for the purpose of cashing government checks in amounts of $1,500 or less if the individual presenting the check is the individual to whom the check has been issued;

(2) which does not require other account relationships with such depository institution;

(3) which does not require the individual to meet any prerequisite which discriminates against low-income individuals in order to use such service;

(4) for which fees, if any, for cashing government checks do not exceed an amount needed to recover all related costs, including fraud losses, as determined by the Board based on actual cost studies;

(5) which allows the customer to designate not less than 3 offices of such depository institution at which such customer may cash government checks upon presentation of—

(A) a copy of the registration provided in accordance with subsection (d) of this section; and

(B) an identification card in the form described in subsection (d)(2)(D) of this section.

(c) EXCEPTION.—A depository institution is not required to provide a government check cashing service under this Act to any individual who has—

(1) a transaction account at any other depository institution, or

(2) a government check cashing relationship at any other depository institution.

(d) REGISTRATION REQUIREMENTS.—

(1) IN GENERAL.—The Board of Governors of the Federal Reserve System shall prescribe such regulations as may be necessary to establish the customer registration program required to use a government check cashing service.

(2) MINIMUM REQUIREMENTS.—Regulations prescribed by the Board under paragraph (1) of this subsection shall contain, at a minimum, the following requirements:

(A) Each depository institution shall provide for registration in all of its deposit taking offices staffed by individuals employed by such depository institution.

(B) Registration shall be by means of an application containing the application date, and the name, address, date of birth, and handwritten signature of the applicant as well as other information the Board determines to be reasonably necessary to facilitate registration of customers for the purpose of this section.

(C) At the time of account registration, an applicant may be required by the depository institution to sign a document in which he states whether he has or has applied for any transaction account or other government check cashing service.

(D) At the time of service registration, an applicant may be required to present an identification card in such form as the Board may require, which includes the signature and a photograph of such customer.

(E) The applicant shall be provided a copy of the completed service registration evidencing the fact that the registration has been received and filed with the depository institution within 15 days of such filing.

(3) REJECTION FOR INTENTIONAL MATERIAL MISREPRESENTATION.—If the depository institution determines that an intentional material misrepresentation has been made in the information required to enable use of a government check cashing service, the depository institution may reject such registration.

(e) INFORMATION ON SERVICE.—Upon request by any individual, a depository institution shall provide such individual with a written summary describing the service offered by such depository institution which meets the requirements of this section.

(f) GOVERNMENT CHECK DEFINED.—For purposes of this section, the term "government check" means any check which was issued by—

(1) the United States, any State, or any agency of the United States; or

(2) any agency of the State in which the check is presented for cashing purposes (in connection with a government check cashing service), any local unit of local government of such State, or any agency of any such unit of local government.

(g) SPECIAL RULE FOR CREDIT UNIONS.—Any credit union which, in the ordinary course of business, cashes checks for members shall cash any government check in an amount of $1,500 or less for any member without charge if the member presenting the check is the individual to whom the check has been issued.

(h) SPECIAL RULE FOR CERTAIN DEPOSITORY INSTITUTIONS.—A depository institution which does not cash checks for customers shall not be required to provide government check cashing services pursuant to this Act.

(i) PREVENTION OF FRAUD LOSSES.—

(1) IN GENERAL.—The Board may, by regulation or order, suspend any requirement of this section for

any classification of checks if the Board determines that—

(A) depository institutions are experiencing an unacceptable level of losses due to check-related fraud with respect to such class of checks; or

(B) there is reasonable cause to believe that such class of checks is being used in a scheme to defraud.

(2) REPORT TO CONGRESS.—Within 10 days of issuing any order or prescribing any regulation under paragraph (1), the Board shall submit a report to the Committee on Banking, Finance and Urban Affairs of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate containing the reason for the order or regulation and the evidence considered in making the determination to issue an order or prescribe a regulation.

(j) CONSUMER RIGHTS.—Notwithstanding any other provision of law, the Board may promulgate regulations to ensure that any individual shall have the right to require that any recurring government check issued to that individual be directly deposited in an account held by that individual in a depository institution, taking into account the safety and soundness of the institutions involved and the efficient operation of the payments system.

SEC. 3. POSTING OF NOTICES.

(a) NOTICE REQUIRED.—Each depository institution shall post a conspicuous notice in the appropriate area of each location where deposits are accepted that informs account holders and potential account holders that government check cashing services are available pursuant to this Act.

(b) CONTENTS OF NOTICE.—Any notice required under subsection (a) shall clearly explain the material features and limitations of government check cashing services, so that customers can reasonably be expected to understand the terms of the service offered.

SEC. 4. ADMINISTRATIVE ENFORCEMENT.

(a) ADMINISTRATIVE ENFORCEMENT.—Compliance with the requirements imposed under this Act and regulations prescribed by the Board under section 6 shall be enforced under—

(1) section 8 of the Federal Deposit Insurance Act—

(A) by the Comptroller of the Currency with respect to national banks;

(B) by the Board with respect to member banks of the Federal Reserve System (other than a national bank); and

(C) by the Board of Directors of the Federal Deposit Insurance Corporation with respect to banks the deposits of which are insured by the

Federal Deposit Insurance Corporation (other than members of the Federal Reserve System);

(2) section 5(d) of the Home Owners' Loan Act of 1933, section 407 of the National Housing Act, and sections 6(i) and 17 of the Federal Home Loan Bank Act, by the Federal Home Loan Bank Board (acting directly or through the Federal Savings and Loan Insurance Corporation) with respect to any depository institution which is subject to any provision of such sections; and

(3) the Federal Credit Union Act, by the National Credit Union Administration Board with respect to any insured credit union.

(b) ADDITIONAL ENFORCEMENT POWERS.—

(1) VIOLATION OF THIS ACT TREATED AS VIOLATION OF OTHER ACTS.—For purposes of the exercise by any Federal depository institutions regulatory agency of any such agency's powers under any Act referred to in subsection (a), a violation of—

(A) a requirement imposed under this Act shall be deemed to be a violation of a requirement imposed under that Act; and

(B) any regulation prescribed by the Board under section 6 shall be deemed to be a violation of a regulation prescribed by such agency under such Act.

(2) ENFORCEMENT AUTHORITY UNDER OTHER ACTS.—In addition to any Federal depository institutions regulatory agency's powers under any provision of law referred to in subsection (a), each such agency may exercise, for purposes of enforcing compliance with any requirement imposed under this Act, any other authority conferred on such agency by any other law.

SEC. 5. CIVIL LIABILITY.

(a) IN GENERAL.—Any depository institution that fails to comply with any requirement imposed under this Act or any regulation adopted pursuant to this Act with respect to any person shall be liable to such person in an amount equal to the sum of—

(1) any actual damage sustained by such person as a result of the failure; and

(2)(A) in the case of an individual action, such additional amount as the court may allow, except that liability under this subparagraph shall not be less than $100 nor greater than $1,000; or

(B) in the case of a class action, such additional amount as the court may allow, except that—

(i) as to each member of the class, no minimum recovery shall be applicable; and

(ii) the total recovery under this subparagraph in any class action or series of class actions arising out of the same failure to comply by the same depository institution shall not be more than the lesser of $500,000 or 1 percent of the net worth of the depository institution.

(b) AMOUNT OF DAMAGES.—In determining the amount of award in any class action, the court shall consider, among other relevant factors—

(1) the amount of any actual damages awarded;

(2) the frequency and persistence of failures of compliance;

(3) the resources of the depository institution;

(4) the number of persons adversely affected; and

(5) the extent to which the failure to comply was intentional.

(c) OTHER RELIEF.—Upon application by an aggrieved party, the appropriate United States district court or any other court of competent jurisdiction may grant such equitable and declaratory relief as is necessary to enforce the requirements imposed under this Act.

(d) COSTS AND FEES.—In the case of any successful action under subsection (a) or (c), the costs of the action, together with a reasonable attorney's fee as determined by the court, shall be added to any damages awarded by the court under such section.

(e) GOOD FAITH RELIANCE.—No provision of this Act imposing liability shall apply to any act done or omitted in good faith in conformity with any official rule, regulation, or interpretation thereof by the Board or in conformity with any interpretation or approval by an official or employee of the Federal Reserve System duly authorized by the Board to issue such interpretations or approvals under such procedures as the Board may prescribe therefor, notwithstanding that after such act or omission has occurred, such rule, regulation, interpretation, or approval is amended, rescinded, or determined by judicial or other authority to be invalid for any reason.

(f) JURISDICTION.—Any action under this section may be brought in the appropriate United States district court without regard to the amount in controversy, or in any other court of competent jurisdiction. No such action shall be brought later than one year after the date of the occurrence of the violation.

SEC. 6. REGULATIONS.

The Board shall prescribe such regulations as it may determine to be appropriate to carry out the provisions of this Act.

SEC. 7. DEFINITIONS.

For purposes of this Act—

(1) FEDERAL DEPOSITORY INSTITUTIONS REGULATORY AGENCY.—The term "Federal depository institutions regulatory agency" means—

(A) the Comptroller of the Currency with respect to national banks;

(B) the Board with respect to member banks of the Federal Reserve System (other than national banks);

(C) the Board of Directors of the Federal Deposit Insurance Corporation with respect to federally insured depository institutions described in clause (i), (ii), or (iii) of section 19(b)(1)(A) of the Federal Reserve Act (other than national banks and member banks of the Federal Reserve System);

(D) the Federal Home Loan Bank Board with respect to federally insured depository institutions described in clause (v) or (vi) of section 19(b)(1)(A) of the Federal Reserve Act; and

(E) the National Credit Union Administration Board with respect to federally insured depository institutions described in clause (iv) of section 19(b)(1)(A) of the Federal Reserve Act.

(2) BOARD.—The term "Board" means the Board of Governors of the Federal Reserve System.

(3) DEPOSITORY INSTITUTION.—The term "depository institution" means any federally insured depository institution described in clauses (i) through (vi) of section 19(b)(1)(A) of the Federal Reserve Act.

(4) STATE.—The term "State" has the meaning given to such term in section 3(a) of the Federal Deposit Insurance Act.

(5) GOVERNMENT CHECK CASHING RELATIONSHIP.—The term "government check cashing relationship" means a relationship between an individual and a depository institution under which a government check cashing service is provided pursuant to section 2(b) of this Act.

(6) TRANSACTION ACCOUNT.—The term "transaction account" has the meaning given such term by section 19(b)(1)(C) of the Federal Reserve Act.

SEC. 8. EFFECTIVE DATE.

This Act shall take effect on the expiration of the date which is 180 days after the date of enactment of this Act.

II

101st CONGRESS
1st Session

S. 907

To provide access to basic banking services.

IN THE SENATE OF THE UNITED STATES

May 3 (legislative day, January 3), 1989

Mr. Metzenbaum introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

---

A BILL

To provide access to basic banking services.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Basic Banking Services Access Act of 1989."

SEC. 2. BASIC FINANCIAL SERVICES ACCOUNT.

(a) Basic Financial Services Account Required.—Each depository institution shall offer a basic financial services account which—

(1) may be used to obtain, at the election of the customer, basic transaction services; and

(2) meets the requirements of this section.

(b) ACCOUNT REGISTRATION.—

(1) IN GENERAL.—The Board of Governors of the Federal Reserve System shall prescribe such regulations as may be necessary to establish the customer registration program required to open a basic financial services account under subsection (a).

(2) MINIMUM REQUIREMENTS.—Regulations prescribed by the Board under paragraph (1) of this subsection shall contain, at a minimum, the following requirements:

(A) Each depository institution shall provide for registration in all of its offices staffed by individuals employed by such depository institution.

(B) Registration shall be by means of an application containing the application date, and the name, address, date of birth, and handwritten signature of the applicant as well as other information the Board reasonably determines to be necessary to facilitate registration of customers obtaining basic transaction services pursuant to this section.

(C) At the time of account registration, an applicant may be required to present an identification card in such form as the Board may require, which includes the signature and a photograph of such customer.

(D) The applicant shall be provided a copy of the completed account registration evidencing the fact that the registration has been received and filed with the depository institution within 15 days of such filing.

(3) REJECTION FOR INTENTIONAL MATERIAL MISREPRESENTATION.—If the depository institution determines that an intentional material misrepresentation has been made in the information provided to open a basic financial services account, the depository institution may reject such registration.

(c) REQUIREMENTS FOR ALL BASIC FINANCIAL SERVICES ACCOUNTS.—No account offered by a depository institution meets the requirement of this section with respect to basic financial services accounts if such account—

(1) requires other account relationships with such depository institution; or

(2) requires the individual to meet any prerequisite which discriminates against low-income individuals in order to open such account.

(d) ACCOUNTS PROVIDING BASIC TRANSACTION SERVICES.—A basic financial services account offered by a depository institution meets the requirements of this section with respect to providing basic transaction services if it is an account—

(1) which is available for such purpose only to individuals (or to members, in the case of a credit union) who have $1,000 or less on deposit at such depository institution;

(2) which the maintenance fee, if any, that includes all service charges and fees for routine transactions, does not exceed the minimal, reasonable amount as established by the Board of Governors of the Federal Reserve based on data submitted from actual time studies and as a reflection of net, processing costs;

(3) which does not have a minimum opening or minimum balance requirement of more than $25;

(4) which, in the case of any depository institution which offers transaction accounts (as defined in section 19(b)(1)(C) of the Federal Reserve Act) in the ordinary course of business, permits checks, share drafts, negotiable orders of withdrawal, or similar instruments to be drawn on the account for purposes of making payments or other transfers to third parties;

(5) which permits not less than 10 withdrawals per month (including withdrawals described in paragraph (4)), whether by check, share draft, negotiable order of withdrawal, or other means;

(6) for which the depository institution is required to provide—

(A) a detailed monthly statement listing all transactions for the month involved; or

(B) a passbook in which the depository institution enters all transactions for such account;

(7) which does not require the individual to exclusively use automated teller machines or other nonteller services for such purpose;

(8) with respect to which, at the election of the individual, the depository institution may allow regularly recurring payments to the individual to be made by the payor to the depository institution for direct deposit into the account of such individual; and

(9) which may be closed after notice to the individual by reason of the occurrence of—

(A) overdrafts with respect to the account of such individual on 3 separate and distinct occasions within any 6-month period; or

(B) a pattern of fraudulent activity involving the account of such individual.

(e) INFORMATION ON ACCOUNTS.—Upon request of any individual, a depository institution shall provide such individual with a written summary describing the account offered by such depository institution which meets the requirements of subsection (a).

SEC. 3. POSTING OF NOTICES.

(a) NOTICE REQUIRED.—Each depository institution shall post a conspicuous notice in the appropriate area of each location where deposits are accepted that informs account holders and potential account holders that basic financial services accounts which provide basic transaction services are available pursuant to this Act.

(b) CONTENTS OF NOTICE.—Any notice required under subsection (a) shall clearly explain the material features and limitations of basic financial services accounts, including basic transaction services, so that customers can reasonably be expected to understand the terms of the account offered.

SEC. 4. ADMINISTRATIVE ENFORCEMENT.

(a) ADMINISTRATIVE ENFORCEMENT.—Compliance with the requirements imposed under this Act and regulations prescribed by the Board under section 6 shall be enforced under—

(1) section 8 of the Federal Deposit Insurance Act—

(A) by the Comptroller of the Currency with respect to national banks;

(B) by the Board with respect to member banks of the Federal Reserve System (other than national banks); and

(C) by the Board of Directors of the Federal Deposit Insurance Corporation with respect to depository institutions insured by the Federal Deposit Insurance Corporation (other than national banks and member banks of the Federal Reserve System);

(2) section 5(d) of the Home Owners' Loan Act of 1933, section 407 of the National Housing Act, and sections 6(i) and 17 of the Federal Home Loan Bank Act, by the Federal Home Loan Bank Board (acting directly or through the Federal Savings and Loan Insurance Corporation) with respect to any depository institution which is subject to any provision of such sections; and

(3) the Federal Credit Union Act, by the National Credit Union Administration Board with respect to any insured credit union.

(b) ADDITIONAL ENFORCEMENT POWERS.—

(1) VIOLATION OF THIS ACT TREATED AS VIOLATION OF OTHER ACTS.—For purposes of the exercise by any Federal depository institutions regulatory

agency of any of such agency's powers under any Act referred to in subsection (a), a violation of—

(A) a requirement imposed under this Act shall be deemed to be a violation of a requirement imposed under that Act; and

(B) any regulation prescribed by the Board under section 6 shall be deemed to be a violation of a regulation prescribed by such agency under such Act.

(2) ENFORCEMENT AUTHORITY UNDER OTHER ACTS.—In addition to any Federal depository institutions regulatory agency's powers under any provision of law referred to in subsection (a), each such agency may exercise, for purposes of enforcing compliance with any requirement imposed under this Act, any other authority conferred on such agency by any other law.

SEC. 5. CIVIL LIABILITY.

(a) CIVIL LIABILITY.—Except as otherwise provided in this section, any depository institution which fails to comply with any requirement imposed under this Act or any regulation prescribed under this Act with respect to any person is liable to such person in an amount equal to the sum of—

(1) any actual damage sustained by such person as a result of the failure;

(2)(A) in the case of an individual action, such additional amount as the court may allow, except that the liability under this subparagraph shall not be less than $100 nor greater than $1,000; or

(B) in the case of a class action, such amount as the court may allow, except that—

(i) as to each member of the class, no minimum recovery shall be applicable; and

(ii) the total recovery under this subparagraph in any class action or series of class actions arising out of the same failure to comply by the same depository institution shall not be more than the lesser of $500,000 or 1 percent of the net worth of the depository institution involved; and

(3) in the case of any successful action to enforce any liability under paragraph (1) or (2), the costs of the action, together with a reasonable attorney's fee as determined by the court.

(b) Class Action Awards.—In determining the total amount of an award in a class action, the court shall consider, among other relevant factors—

(1) the amount of any actual damages awarded;

(2) the frequency and persistence of failures of compliance;

(3) the resources of the depository institution;

(4) the number of persons adversely affected; and

(5) the extent to which the failure of compliance was intentional.

(c) BONA FIDE ERRORS.—

(1) GENERAL RULE.—A depository institution may not be held liable in any action brought under this section for a violation of this Act if the depository institution demonstrates by a preponderance of the evidence that the violation was not intentional and resulted from a bona fide error, notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.

(2) EXAMPLES.—Examples of a bona fide error include clerical, calculation, computer malfunction and programming, and printing errors. An error of legal judgment with respect to a depository institution's obligation under this Act is not a bona fide error.

(d) JURISDICTION.—Any action under this section may be brought in any United States district court, or in any other court of competent jurisdiction, within one year after the date of the occurrence of the violation involved.

(e) RELIANCE ON BOARD RULINGS.—No provision of this section imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule, regulation, or interpretation thereof by the Board, or in conformity with any interpretation or approval by an official or employee of the Federal Reserve System duly authorized by the Board to issue such interpretation or approval under procedures prescribed by the Board, notwithstanding, the fact that after such act or omission has occurred, such rule, regulation, interpretation, or approval is amended, rescinded, or determined by judicial or other authority to be invalid for any reason.

(f) NOTIFICATION OF AND ADJUSTMENT FOR ERRORS.—A depository institution shall not be liable under this section or section 4 for any failure to comply with any requirement imposed under this Act with respect to any account if—

(1) before—

(A) the end of the 60-day period beginning on the date on which the depository institution discovered the failure to comply;

(B) any action is instituted against the depository institution by the account holder under this section with respect to such failure to comply; and

(C) any written notice of such failure to comply is received by the depository institution from the account holder, the depository institution notifies the account holder of the failure of such institution to comply with such requirement; and

(2) the depository institution makes such adjustments as may be necessary with respect to such account to ensure that—

(A) the account holder will not be liable for any amount in excess of the amount actually disclosed with respect to any fee or charge;

(B) the account holder will not be liable for any fee or charge imposed under any condition not actually disclosed; and

(C) interest on amounts in such account will accrue at the annual percentage yield, and under the conditions, actually disclosed (and credit will be provided for interest already accrued at a different annual percentage yield and under different conditions than the yield or conditions disclosed).

(g) MULTIPLE INTERESTS IN 1 ACCOUNT.—If more than 1 person holds an interest in any account—

(1) the minimum and maximum amounts of liability under subsection (a)(2)(A) for any failure to comply with the requirements of this Act shall apply with respect to such account; and

(2) the court shall determine the manner in which the amount of any such liability with respect to such account shall be distributed among such persons.

(h) CONTINUING FAILURE TO DISCLOSE.—

(1) CERTAIN CONTINUING FAILURES TREATED AS 1 VIOLATION.—Except as provided in paragraph (2), the continuing failure of any depository institution to disclose any particular term required to be disclosed under this Act with respect to a particular account shall be treated as a single violation for purposes of determining the amount of any liability of such institution under subsection (a) for such failure to disclose.

(2) SUBSEQUENT FAILURE TO DISCLOSE.—The continuing failure of any depository institution to disclose any particular term required to be disclosed under this Act with respect to a particular account after judgment has been rendered in favor of the account holder in connection with a prior failure to disclose such term shall be treated as a subsequent violation for purposes of determining liability under subsection (a).

SEC. 6. REGULATIONS.

The Board shall prescribe such regulations as such agency may determine to be appropriate to carry out the provisions of this Act.

SEC. 7. DEFINITIONS.

For purposes of this Act—

(1) APPROPRIATE FEDERAL DEPOSITORY INSTITUTIONS REGULATORY AGENCY.—The term "appropriate Federal depository institutions regulatory banking agency" means—

(A) the Comptroller of the Currency with respect to national banks;

(B) the Board with respect to member banks of the Federal Reserve System (other than national banks);

(C) the Board of Directors of the Federal Deposit Insurance Corporation with respect to federally insured depository institutions described in clause (i), (ii), or (iii) of section 19(b)(1)(A) of the Federal Reserve Act (other than national banks and member banks of the Federal Reserve System);

(D) the Federal Home Loan Bank Board with respect to federally insured depository institutions described in clause (v) or (vi) of section 19(b)(1)(A) of such Act; and

(E) the National Credit Union Administration Board with respect to federally insured depository institutions described in clause (iv) of section 19(b)(1)(A) of such Act.

(2) **Board.**—The term "Board" means the Board of Governors of the Federal Reserve System.

(3) **Depository institution.**—The term "depository institution" means any federally insured depository institution described in clauses (i) through (vi) of section 19(b)(1)(A) of the Federal Reserve Act.

(4) **State.**—The term "State" has the meaning given to such term in section 3(a) of the Federal Deposit Insurance Act.

SEC. 8. EFFECTIVE DATE.

This Act shall take effect on the expiration of the date which is 90 days after the date of the enactment of this Act.

II

101st CONGRESS
1st Session

S. 909

To amend the Community Reinvestment Act of 1977 to require written evaluations.

IN THE SENATE OF THE UNITED STATES

May 3 (legislative day, January 3), 1989

Mr. Metzenbaum introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

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A BILL

To amend the Community Reinvestment Act of 1977 to require written evaluations.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. COMMUNITY REINVESTMENT ACT.

The Community Reinvestment Act of 1977 (12 U.S.C. 2901 et seq.) is amended by adding at the end the following:

"SEC. 807. WRITTEN EVALUATIONS.

"(a) Required.—

"(1) In general.—Upon the conclusion of each examination of a financial institution under section 804, the appropriate Federal financial supervisory agency shall prepare a written evaluation of the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods.

"(2) PUBLIC AND CONFIDENTIAL SECTIONS.—Each written evaluation required under paragraph (1) shall have a public section and a confidential section.

"(b) PUBLIC SECTION OF REPORT.—

"(1) FINDINGS AND CONCLUSIONS.—The public section of the written evaluation shall—

"(A) state the appropriate Federal financial supervisory agency's conclusions for each assessment factor identified in the regulations prescribed by the Federal financial supervisory agencies to implement this Act; and

"(B) discuss the facts supporting such conclusions.

"(2) EMPHASIS ON SPECIFIC TYPES OF CREDIT.—The statement, discussion, supporting facts, and conclusions shall place special emphasis on the regulated financial institution's record of serving the housing credit needs of low- and moderate-income persons, small business credit needs, and small farm credit needs.

"(3) ASSIGNED NUMERICAL RATING.—The public section shall also contain the institution's numerical rating, as required by the regulations implementing the Community Reinvestment Act of 1977 in effect on the date of enactment of this section.

"(c) CONFIDENTIAL SECTION OF REPORT.—

"(1) PRIVACY OF NAMED INDIVIDUALS.—The confidential section of the written evaluation shall contain all references that identify any customer of the institution, any employee or officer of the institution, any person or organization that has provided information in confidence to a Federal financial supervisory agency.

"(2) OTHER TOPICS NOT SUITABLE FOR DISCLOSURE.—The confidential section shall also contain any inflammatory statements or other such statements which, in the judgment of the appropriate Federal financial supervisory agency, are not properly subject to disclosure to the institution or the public.

"(3) NONDISCLOSURE TO DEPOSITORY INSTITUTION.—The confidential section shall not be disclosed to the institution or the public, unless the appropriate Federal financial supervisory agency determines that such disclosure would be in the public interest.".

Senator **Dixon**. Well, may I say we thank the distinguished Senator from Ohio for his testimony this morning. It is customary in these situations to invite the sponsors of legislation to participate if they care to in the hearing. I know that the Senator is a busy man, but if he would care to join us for a while and ask questions of some of the witnesses, I'm sure no one on the committee would have any objection to that.

Senator **Metzenbaum**. I will do that, Mr. Chairman.

Senator **Dixon**. My colleague and friend, the distinguished Senator from New York State is here. I wonder if he has any statement before we have the panels this morning.

Senator **D'Amato**. Mr. Chairman, I do. In the interest of time, I would ask that my statement be included in the record as if read in its entirety.

STATEMENT OF SENATOR D'AMATO

Senator **D'Amato**. Mr. Chairman, I am pleased to join you in convening this first meeting of the Consumer Subcommittee. I congratulate you upon taking up these controversial bills early on your agenda. I am particularly interested in the issues raised by the two bills before us today.

The availability of the basic financial services to the poor is surely a matter of concern to every member of the Banking Committee if not every member of Congress.

I would like to offer two thoughts on the process of consumer banking legislation. First, if there is a problem here, let us address it. If there is a consumer demand for basic banking services at low cost or if government checks are not being cashed we should address those issues. But we should avoid simply treating this as a problem with only a legislative solution. If there is another approach that will provide better service to the consumer, this is the time and the place to raise it.

The need to look at alternatives to legislative action brings me to my second point. There are a few encouraging signs that cooperation between consumer advocates and financial service companies can address some of the difficult consumer banking problems. I welcome those signs. This, of course, if preferable to continued legislative confrontations for a number of reasons. Cooperative, good faith negotiations between banks and the people they serve are far more efficient and effective in delivering the services which consumer really need. The result of such negotiations can address local conditions which can vary greatly from one locale to another.

While the market mechanism is not perfect it should certainly be a factor in designing any service. Local action can address a local market. I have far greater faith in such action than in the ability of those here in Washington to identify one or two banking services that will provide a meaningful improvement in the financial services available to the poor throughout the country.

To those who testify here today I would commend the cooperative approach—the public/private partnership if you will—to providing better services to low income consumers. It can only improve the lot of consumers to have businesses and consumer advocates work together toward goals that will benefit the people who should be the beneficiary of their common efforts, the customer.

I would say this, Mr. Chairman, without getting into the merits of S. 907 or S. 909, which I have not had an opportunity to, I am myself very sympathetic. It seems to me that as it relates to S. 906, we should look to work out whatever differences that staff and others might have and see to it that we address that issue. That's always been something that's troubled me for many years. There's no reason not to get the government checks on the Federal, State and local level accepted and we find that people go through all kinds of contrivances, et cetera, to get it taken place or others to keep it from taking place.

So the intent of S. 906 I believe is something we should all be able to agree on.

Senator METZENBAUM. That's very encouraging news from the Senator from New York and I certainly look forward to working with him in connection with this legislation.

Senator DIXON. Thank you, Senator.

Before we begin, I have a statement from Senator Kerry that is to be inserted in the record.

STATEMENT OF SENATOR KERRY

Senator KERRY. I commend you for calling these hearings and for focusing the attention of the committee upon a rapidly evolving area of federal policy that is likely to assume dramatically increased importance in the coming years.

While many have criticized the effectiveness of the Community Reinvestment Act, those critics have usually overlooked the core significance of the CRA. Reversing prior dogma, the CRA has by now firmly established the principle that federally chartered and insured banks and thrifts have an affirmative obligation to serve their communities. Thanks to the Act, many low-income minority and inner-city communities are being presented with an opportunity: previously denied to them, to finance housing improvements, small business, and economic developments.

Their financing skills and knowledge of local markets has always rendered the participation of banks essential to effective community re-development efforts. The importance of their effective participation is, however, unmistakeable in light of the unprecedented fiscal constraints now facing the U.S. government. For its part, government at all levels must ensure that inadequate infrastructure does not impede otherwise favorable lending opportunities in disinvested communities. Where it can be effective, and where necessary resources can be found, government must also provide incentives that make community redevelopment lending more attractive to bankers, for clearly, we cannot impose upon depository institutions alone the burdens to invest in and sustain areas of our country which other businesses and investors have cast aside.

But while it is a significant achievement, the great promise of the CRA remains largely unfulfilled. To long-neglected inner-city, minority, and low-income communities, the CRA provides real hope for gradual improvements in their housing, education, health care, and for expanded economic opportunity. By fostering real and lasting improvements in these communities, the CRA can also reduce the continuous and futile government expenditures to alleviate the consequences of inadequate housing, poor health care and sanitation, and inadequate education. I look forward to the testimony of the distinguished panel of witnesses assembled here today.

Thank you, Mr. Chairman.

Senator DIXON. Ladies and gentlemen, the first panel will consist of Howard Brown, the Banking Commissioner of the State of Connecticut—incidentally, in the event that Senator Dodd can't be here—he had a speaking engagement this morning and he asked me to express to the commissioner his welcome to the committee for being here this morning. He will be here during the course of the hearing. Mr. W.E. Douglas, the Commissioner of the Financial Management Service in the Treasury Department, thank you for being here, Mr. Douglas. Mr. Gerry Gagerman, president, National Clearings Inc., of Chicago, and president of the National Check Cashers Association, and we thank you for being here, Mr. Gagerman. And Rosemary Dunlap, Virginia Citizens Consumer Council.

Now I hope Ms. Dunlap will forgive me for going with one of the gentlemen first, but I think I'll do it in the order that my staff has listed these witnesses and we will greatly appreciate it if you would place your full statement in the record and confine your remarks to seven minutes each. I think there's an indicator up here that will show you when your time has expired.

Mr. Brown, we are delighted to have you.

STATEMENT OF HOWARD B. BROWN, BANKING COMMISSIONER, STATE OF CONNECTICUT

Mr. BROWN. Thank you, Mr. Chairman.

Senator Metzenbaum, distinguished members of the Subcommittee on Consumer and Regulatory Affairs, my name is Howard Brown. I am Banking Commissioner of the State of Connecticut. It is with great pleasure that I address you today and I am particularly pleased to have been invited to testify about the experiences my State has had in adopting legislation regarding government check cashing and check-cashing centers.

PUBLIC ACT 87-24

Fortunately, in Connecticut, we are well-equipped with laws that govern the manner by which banking institutions provide services to all State residents.

One of those laws, Public Act 87-24, enacted in 1987, requires all Connecticut banking institutions, both State and federally chartered, to cash State public assistance checks for any recipient payee who endorses the check and offers reasonable identification.

Recipients are largely single mothers with small children, the blind, the disabled and the elderly who often have difficulty getting to a bank at all.

Public Act 87-24 prohibits banks from charging public assistance recipients for cashing these checks and requires them to cash the checks regardless of whether the person negotiating the check has an account with the banking institution.

I should also point out that our law applies to State and federally chartered credit unions as well, but only if that person to whom the check is issued is a credit union member, similar to the bill introduced by Senator Metzenbaum.

BACKGROUND OF THE LAW

Let me recount how our current law came to be adopted. In 1985, as Deputy Banking Commissioner, I served as a member of an ad hoc committee which studied the issue of lifeline banking within Connecticut. I consider welfare check cashing to be one of the components of lifeline banking. The practice at the time had been to allow banks to set their own policies regarding the cashing of public assistance checks.

Some of the banks concerned about fraud adopted restrictive policies toward cashing public assistance checks. These policies, in turn, placed an undue burden on banks that were willing to cash the checks and on public assistance recipients who in some instances had to travel considerable distances to cash a check when there was a bank around the corner from their home but of course had a restrictive check-cashing policy.

Pressure to alleviate this situation mounted when a number of check-cashing companies began to crop up to take over where the banks were not meeting the need for public assistance recipients. The question often asked was, "Why should the working poor or welfare recipients have to pay $5 or $10 to get a check cashed?" Banks, after all, are chartered by the State and they ought to serve all residents unless what is being requested is legitimately cost prohibitive.

Having determined that there were people relying on government benefit checks who were having an extremely difficult time cashing those checks at some banks, I recommended that all banks honor State public assistance checks.

In 1986, a mandatory check-cashing measure was proposed by the Connecticut State Legislature but was not enacted when questions arose concerning the cost of fraudulent checks. Lawmakers were unable to agree on whether the state or the banks should cover those costs.

A year later, the banks committee of the Connecticut General Assembly introduced similar legislation which this time met with little resistance from bankers. SHB 5558, an act concerning cashing State checks, passed the House of Representatives by a margin of 145 to 1 and was unanimously passed in the Senate.

The issue dealing with the cost of fraudulent checks had been resolved. Under our law, banks are not liable to reimburse the State of Connecticut for any loss incurred as a result of wrongful payment of a public assistance check as long as they have followed certain rules outlined by regulation. Those regulations which went into effect in October 1988 standardized a number of procedures the banking community had already put into practice since passage of the law in 1987.

The regulations clearly outline the procedure that must be followed when cashing the checks. The procedures, I believe, provide adequate control while not being overly burdensome to the banks.

To recap the regulations briefly, public assistance checks must be cashed in person by the payee with two forms of identification, which together show a signature, a photograph and a unique identifying number. I am pleased to report here today that no significant problems either for the banks or for the individuals cashing the checks have been noted by my agency.

In February, on my instruction, an on-site visit by bank examiners to various bank offices located in our larger metropolitan areas found that bank employees are acting responsibly and in compliance with the law and regulations.

The Connecticut Department of Banking has also attempted to explain the new standards to Connecticut residents affected by the law and regulations. News releases and public service announcements have been generated to media representatives in all areas of the State.

Last week I asked my agency staff to conduct a follow-up survey of our larger metropolitan area banking institutions to ascertain if they have encountered any problems since our initial survey. It appears that the results have been successful. The check-cashing needs of public assistance recipients continue to be met in a dignified and orderly fashion without any detrimental impact on the banks.

Losses from fraudulent checks have been minimal and when such losses have been submitted for payment to the Connecticut Department of Income Maintenance reimbursements have been made in a timely fashion.

Furthermore, I'm told that public assistance recipients continue to become more aware of the check-cashing system which banks have instituted.

Since all banks now adhere to the same check-cashing policies as to these instruments as required by law, the volume of public assistance checks cashed in any one bank has been decreased. Connecticut is haled as being the first in the country to pass legislation that requires all banks to cash public assistance checks. It is vital for us to recognize the need to extend to public assistance recipients the benefits of affordable banking services the rest of us enjoy and take for granted.

An issue which goes hand-in-hand with government check-cashing is the recent proliferation in our metropolitan areas of privately owned check-cashing centers. Before the need for welfare assisted residents were fully met by banking institutions in response to the governmental check-cashing law I outlined earlier, many of them along with the working poor, were inclined to patronize these unregulated check-cashing companies.

The chairman of our legislature's banking committee and I personally visited a number of these outlets during the summer of 1988 to determine how much they were charging customers for the check-cashing services. We found that the centers cashed checks for fees of anywhere from 1½ percent to 6 percent and more of the face value of the instrument. That same summer, a 3.7 percent increase in public assistance benefits went into effect.

Senator DIXON. I'll have to ask you to conclude, Mr. Brown. It's very interesting and we have a lot of questions, but I'm going to have to ask you to conclude.

Mr. Brown. Thank you, Senator. That's basically my conclusion. I had a flowery last paragraph, but I don't think I need to read that to you.

Senator Dixon. Well, I hate to miss that, but we want to get some questions answered by you. It's a very interesting thing you're experiencing in Connecticut.

[The complete prepared statement of Howard B. Brown follows:]

STATE OF CONNECTICUT
DEPARTMENT OF BANKING
44 CAPITOL AVENUE • HARTFORD, CT 06106

Howard B. Brown
Commissioner

TESTIMONY OF

HOWARD B. BROWN

BANKING COMMISSIONER, STATE OF CONNECTICUT

before the

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

of the

SENATE COMMITTEE ON BANKING, HOUSING

AND URBAN AFFAIRS

June 6, 1989

Mr. Chairman, and distinguished members of the Subcommittee on Consumer and Regulatory Affairs, my name is Howard B. Brown. I am Banking Commissioner of the State of Connecticut.

It is with great pleasure that I address you today and I am particularly pleased to have been invited to testify about the experiences my state has had in adopting legislation regarding government check cashing and check cashing centers.

As Banking Commissioner, my responsibility is to protect the citizens of Connecticut by insuring the safety and soundness of our financial institutions. To uphold this charge means not only protecting the funds which consumers place in the hands of our banking institutions, but, of equal importance, protection for consumers against any banking practices which infringe on the inherent rights of any consumer.

Fortunately, in Connecticut we are well equipped with laws that govern the manner by which banking institutions provide services to all state residents. One of those laws, Public Act 87-24, enacted in 1987, requires all Connecticut banking institutions, both state and federally-chartered, to cash state public assistance checks for any recipient who endorses the check and offers reasonable identification. Public assistance recipients affected are people receiving assistance under Aid to Families with Dependent Children, the State Supplement, Medicaid, or the Refugee Program.

Recipients are largely single mothers with small children, the blind, the disabled and the elderly, who often have difficulty getting to a bank at all, let alone a bank that will honor their checks.

Public Act 87-24 prohibits banks from charging public assistance recipients for cashing these checks and requires them to cash the checks regardless of whether the person negotiating the check has an account with the banking institution. I should also point out that our law applies to state and federally-chartered credit unions as well, but only if the person to whom the check is issued is a credit union member.

Let me recount how our current law came to be adopted. In 1985, as Deputy Banking Commissioner, I served as a member of an Ad Hoc committee that studied the issue of lifeline banking within Connecticut. I consider welfare check-cashing to be one of the components of lifeline banking. The practice, at the time, had been to allow banks to set their own policies regarding the cashing of public assistance checks. Some of the banks, concerned about fraud, adopted restrictive policies toward cashing public assistance checks. Those policies, in turn, placed an undue burden on banks that were willing to cash the checks and on public assistance recipients who, in some instances, had to travel considerable distances to cash a check when there was a bank around the corner from their home.

Pressure to alleviate this situation mounted when a number of check-cashing companies began to crop up to take over where the banks were not meeting the needs of public assistance recipients. The question often asked was: "Why should the working poor or welfare recipients have to pay $5 or $10 to get a check cashed?" Banks, after all, are chartered by the state and they ought to serve all residents.

Having determined that there were people relying on government benefit checks who were having an extremely difficult time cashing those checks at some banks, I recommended that all banks honor state public assistance checks.

In 1986, a mandatory check-cashing measure was proposed by the Connecticut state legislature but was not enacted when questions arose about the cost of fraudulent checks. Lawmakers were unable to agree on whether the state or the banks would have to cover those costs.

A year later, the Banks Committee of the Connecticut General Assembly introduced similar legislation which this time met with little resistance from bankers. SHB 5558, An Act Concerning Cashing State Checks, passed the House of Representatives by a margin of 145 to 1 and was unanimously passed in the Senate.

The issue dealing with the cost of fraudulent checks had been resolved. Under our law, banks are not liable to reimburse the State of Connecticut for any loss incurred as a result of wrongful payment for a public-assistance check as long as they have followed the rules outlined in regulations promulgated by the Connecticut Department of Income Maintenance in cooperation with the Department of Banking.

Those regulations, which went into effect in October of 1988, standardized a number of procedures the banking community had already put into practice since passage of the law in 1987. The regulations clearly outline the procedures that must be followed when cashing the checks. The procedures I believe provide adequate control while not being overly burdensome to the banks.

To recap the regulations briefly, public-assistance checks must be cashed in person and two forms of identification which together show a signature, photograph and unique identifying number are required. Acceptable forms of identification include a Connecticut's driver's license, a Department of Income Maintenance public assistance card; a credit card, bank card, union card or any other valid ID. The bank that cashes the check is required to record the information on the back of the check as evidence that it followed the established procedure.

I am pleased to report here today that no significant problems either for the banks, or for the individuals cashing the checks, have been noted by my agency. In February, on my instruction, an on-site visit by bank examiners to various bank offices located in our large metropolitan areas found that bank employees are acting responsibly and in compliance with the law and regulations. Based on information reported to me, there was no case noted in which a bank refused to cash a check when adequate identification was presented. In instances where customers did not always have current IDs and were not aware of the new requirements, Connecticut banking institutions appear to have generally exercised good judgment and cooperation in such situations by trying to properly inform individuals of the recently enacted law.

The Department of Banking has also attempted to explain the new standards to Connecticut residents affected by the law and regulations. News releases and public service announcements have been generated to media representatives in all areas of the state.

Last week, I asked my agency staff to conduct a follow-up survey of our large metropolitan-area banking institutions to ascertain if they have encountered any problems since our initial survey. It appears that the results have been successful. The check cashing needs of public assistance recipients continue to be met in a dignified and orderly fashion without any serious financial or operational impact on the banks. Losses from fraudulent checks have been minimal, and when such losses have been submitted for payment to the Department of Income Maintenance, reimbursement has been made in a timely fashion.

Furthermore, I'm told that public assistance recipients continue to become more aware of the check cashing system which banks have instituted. Since all banks now adhere to the same check cashing policies required by law, the volume of public assistance checks cashed in any one bank has been decreased.

Connecticut is heralded as being the first in the country to pass legislation that requires all banks to cash public assistance checks. It is vital for us to recognize the need to extend to public assistance recipients the benefits of affordable banking services the rest of us enjoy. As Connecticut's Banking Commissioner, I am pleased to be part of a government network that is continually looking out for the interests of all our residents.

An issue which goes hand in hand with governmental check cashing is the recent proliferation in our metropolitan areas of privately-owned check cashing centers. Before the needs of welfare assisted residents were fully met by banking institutions in response to the governmental check cashing law I outlined earlier, many of them, along with the working poor, were inclined to patronize these unregulated check cashing companies.

The chairman of our legislative Banks Committee and I personally visited a number of these outlets during the summer of '88 to determine how much they were charging customers for the check cashing services. We found that the centers cashed checks for fees of anywhere from 1 1/2 per cent to 6 per cent of their face value. That same summer a 3.7 per cent increase in public assistance benefits went into effect. We asked ourselves, what's the point of the increase if it winds up in the hands of a check cashing center?

It was that kind of thinking which prompted the legislature earlier that year to seek a remedy for the situation. Public Act 88-200, An Act Concerning Check Cashing Services, went into effect October 1, 1988 authorizing the Commissioner of Consumer Protection to regulate these check cashing services. The law not only required the centers to be licensed but set a rate a check center can charge for cashing a check at three-fourths of 1 per cent, plus a handling charge of 10 cents a check or 30 cents a transaction.

The adoption of that legislation triggered a class action suit filed by several check cashing companies operating in Connecticut. Litigation is still pending and a U.S. District Court judge had stayed enforcement of the rate cap pending the outcome of the trial.

This month, the Connecticut General Assembly passed a new bill which transfers jurisdiction over check cashing firms from the state Department of Consumer Protection to the Department of Banking, and requires those companies to cash state public assistance checks at a fee of not more than 1 per cent of their face value. The bill also eliminates the three-fourths of 1 per cent cap imposed earlier on the firms' general check cashing services.

This new legislation, SHB 5202 (PA 89-178), does not establish a general check-cashing fee, rather it requires me to adopt regulations before October 1, 1989, establishing the maximum fees a licensed check cashing business may charge for cashing a check, draft, or money order drawn on a depository institution. In establishing maximum fees, I have been asked to consider the effect any rate changes will have on consumers, start-up costs, operational expenses, volume of business, and any other information deemed relevant.

I have asked the General Assembly to enact an amendment to this bill which will require every check cashing company to provide me with a certified financial statement.

To date, there are seven check cashing companies operating one or more offices in Connecticut.

I thank you for giving me the opportunity to be here today in order to personally share the experiences the state of Connecticut has encountered in the area of mandatory state government check-cashing and the advances we are continually making to resolve the problems associated with check cashing companies.

HARTFORD COURANT July 14, 1989

Check centers should not cash in on poor

Tom Condon

The tall, slender, black man walked up to the counter of the Connecticut State Check Cashing Services store on Albany Avenue and asked to cash a money order.

"I don't cash any money orders except my own," replied the stocky, feisty white man behind the counter, who identified himself as Bob.

"But Bob," said the customer, looking around, "there's no sign posted about that."

Bob produced a sign from behind the counter. The customer asked if he could cash a certified check and was told the center only cashed government and payroll checks. The customer asked why.

"Hey, I see 3,000 people a week. I don't have to listen to you," said Bob, angrily. "I told you everything I'm going to tell you."

For now. The customer was state Banking Commissioner Howard B. Brown Jr. Brown and other state officials are about to put the squeeze on check-cashing centers.

Brown and State Rep. Thomas D. Ritter, D-Hartford, House chairman of the General Assembly's banks committee, took a ride around Hartford Monday to visit the city's newest growth industry. I invited myself along.

In the past 2½ years, a half-dozen check-cashing centers have cropped up in the city, mostly in poor neighborhoods. Another dozen or so have appeared in Bridgeport, New Haven and Waterbury.

The centers are kind of ersatz banks for people who don't have bank accounts. The centers cash checks for fees of anywhere from 1½ percent to 10 percent of their value. They also sell money orders, and some of them sell lottery tickets.

Ritter and Brown feel the check-cashing centers exploit poor people. They helped initiate two laws that are about to make life anxious for check-center owners.

The first, passed last year, will require all banks to cash welfare checks for free.

Brown said he did a survey and found that only about 55 percent of area banks were offering services for poor people such as free checking or cashing welfare checks. He said some banks cash welfare checks at certain branches and not others.

"As the banking industry moves toward more sophisticated financial services for their upscale clientele, they're squeezing out the little guys," he said.

That law is to take effect when the Department of Income Maintenance completes the regulations for it, which are expected in the fall.

On Oct. 1, another law, passed this year, is to take effect. This law will set the rate a check center can charge for cashing a check at three-fourths of 1 percent, plus a handling charge of 10 cents a check or 30 cents a transaction.

The owners claim Ritter slipped this bill past them, and are furious. They've hired two big hitters, lobbyist Patrick Sullivan and New York lawyer Jerry Goldman to get the Connecticut law changed.

"If nothing happens between now and Oct. 1, the whole industry in Connecticut closes down," said Michael V. Vizzielo, president of Cash-a-Check Inc. of New Haven.

"We just can't stay in business at that rate," said Michael Rose, executive vice president of Connecticut State Check Cashing Services.

Vizzielo said his centers are "good for the people." He said he's in neighborhoods where banks won't open, and said he takes risks banks don't take. "Before the check-cashing centers, people had to cash checks in gin mills or package stores, or have 25 kinds of ID at banks," he said.

"My place looks like a bank. I require no ID. I say, 'Good Morning, Mrs. Jones, what can I do for you?' I give the people dignity," he said.

He's right that some banks have made it tough for poor people by not cashing welfare checks and by closing branches in poor neighborhoods.

But poor people shouldn't have to pay $5 or $10 to get a check cashed. Banks are chartered by the state and ought to serve all state residents.

On July 1, a 3.7 percent increase in welfare benefits went into effect. What is the point if the increase goes to a check-cashing center?

I suspect the centers can live on three-fourths of 1 percent, as their New York counterparts do.

Francisco Ortiz, a customer at the Check Cashing Store on Park Street, said the place was doing a brisk business.

"He's making a killing," said Ortiz. "He's making more than the package store."

Write to Tom Condon in care of The Courant, 285 Broad St., Hartford 06115

Senator DIXON. Mr. Douglas.

STATEMENT OF WILLIAM E. DOUGLAS, COMMISSIONER, THE FINANCIAL MANAGEMENT SERVICE, DEPARTMENT OF THE TREASURY

Mr. DOUGLAS. Thank you, Mr. Chairman.

Mr. Chairman, I welcome this opportunity to talk about the role of the Financial Management Service in providing benefit payments to tens of millions of taxpayers. I will submit my statement for the record and just take a moment or two of the committee's time to highlight several points.

The Financial Management Services makes over 750 million payments each year to taxpayers and citizens of this country. About 450 million of those payments are made by check, Mr. Chairman, and the balance are made electronically through the direct deposit program made through automated clearing houses.

We are supportive of the intent of S. 906 because we believe that any measure which will result in improved service to recipients of government checks is desirable.

We do, however, have some concerns about emphasizing and encouraging more checks. The price of forgery to the American taxpayer is substantial. Last year, we reclaimed $68 million from banks and businesses because they honored checks with forged or improper endorsements. The Financial Management Service is looking for ways to improve the delivery of benefit payments to recipients without encountering those sorts of problems and we've had a lot of experience with lost checks and stolen and forged checks.

Each year, we receive somewhere between 1.5 million and 1.8 million initial claims of nonreceipt of checks and many of those turn out simply to be delayed or people have forgotten they've gotten them, but many of these claims involve with truly lost or stolen and forged checks.

The risk of a check recipient not getting their benefit check on time is 1500 percent greater than direct deposit recipients.

In addition to that, if a check is lost or stolen, the amount of time it takes to determine what has happened and, if necessary, replace that check can range from, at best, three weeks to frequently 3, 4 months and sometimes longer when complex field investigations by Secret Service is required.

On the other hand, with direct deposit, when a payment—and that happens occasionally—is misapplied to an account or goes to a different financial institution, it usually takes us 24 to 48 hours to determine the problem and correct it and get the money in the hands of the people.

So we believe that the electronic payment answer is much superior to the check payment approach.

This fall we will start a test with the Social Security Administration using SSI recipients who are unbanked—do not have a banking relationship. They will be volunteers. It will be in the city of Baltimore, three zip codes in the inner city, and we are going to provide them with a plastic card, an access card, by which they can get their benefit payments through either ATM's or point of sale terminals in retail establishments. They can draw down the entire amount at one time or they can draw down a smaller amount and go back again for additional funds, just as you would write a check. It's an electronic letter of credit if you want to use that sort of term.

We believe that the future for electronic benefit payments is far brighter than to continue to emphasize check delivery, and so we would ask that the committee look at a number of options as it faces this issue that has been raised by Senator Metzenbaum and which obviously identifies a real problem facing the citizens of the country.

That's the conclusion of my summation, Mr. Chairman.

[The complete prepared statement of William E. Douglas follows:]

TESTIMONY OF
WILLIAM E. DOUGLAS
COMMISSIONER, THE FINANCIAL MANAGEMENT SERVICE
DEPARTMENT OF THE TREASURY
BEFORE
THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
SENATE COMMITTEE ON BANKING

JUNE 6, 1989

Mr. Chairman, I welcome the opportunity to discuss some of the important roles performed by the Financial Management Service on behalf of the Federal Government and the taxpayers of this country.

Although financial management is not a high visibility activity in the Government, there are few activities which are more vital to the well-being of the country. We are Government's principal money manager overseeing the largest cash flow in the world - approximately $2 trillion each year. Our responsibilities encompass a full range of financial functions in payments, collections, cash management, credit and debt management, financial systems, government-wide accounting and general financial services. In addition to performing these duties, we are one of the Government's major profit centers. For every $1.00 appropriated to us, we earn $10.00 -- and each year this profit margin grows. In FY 1988 it was a total of $2.8 billion.

Mr. Chairman, among our essential roles is responsibility for making 750 million payments each year. Fifteen years ago, the Financial Management Service used a costly, labor intensive and paper based system for making the Government's payments. Since that time we have worked to develop systems which ensure rapid, reliable, and safe delivery of payments to our citizens who depend upon these payments. The result has been an evolving payment process which has not only moved steadily toward our first goal, safety, security and reliability, but has also reduced the costs to the American taxpayer for this service.

In general, the Financial Management Service is turning the Government away from a reliance on costly, error-prone, paper financial transactions, and is making it an acknowledged leader in the use of electronic financial systems. This approach has not only greatly improved the quality and magnitude of the services we provide, it has allowed us to expand substantially our responsibilities and workload. We have done these things with essentially a flat budget (in constant 1980 dollars) throughout this decade, and with 22 % fewer employees than we had at the beginning of the period.

The check is an imperfect and, in some cases, an unreliable payment medium. We have moved towards increased use of electronic payments such as Direct Deposit because they are electronic payments such as Direct Deposit because they are delivered more quickly, reliably, and safely. The fact that such payments are also much less costly is a bonus.

We have examined the proposed legislation with much interest, and we commend its intent, for it mirrors our concern - ensuring that people receiving Government payments have access to these funds promptly. That concern drove us to initiate the use of Direct Deposit payments. First, and foremost, they are safe and reliable. Second, they are cost effective. And, third, the funds are "available" to the recipient more quickly.

Although the Administration has not formulated a position on S.906, I would be remiss if I did not voice some of the concerns which have been evolving over recent years about the check payment process. This legislation is concerned with payment recipients who are "unbanked", yet present conditions have made checks a questionable payment technique in certain parts of the country.

We have discovered through unpleasant experience that there is a growth industry of people who steal Government checks and cash them through various means. We know, for instance, by analysis of the nearly 1.8 million initial claims of late or undelivered checks, that a disproportionate percentage of non-receipt claims come from urban locations where a large number of unbanked

recipients reside. Rural and suburban locations do not share this problem to the same degree.

It is our view, therefore, requiring all banks to cash Government-issued checks is, at best, only a partial solution to the larger problem. Requiring would-be check cashers to produce an identification card will probably be most useful in smaller communities and rural areas, but those are also the locations where the stolen and forged check industry is not active, and bank personnel are more likely to know area residents even if they are not customers of the bank.

On the other hand, should this Bill become law, it seems reasonable to assume that "market demand" for counterfeit cards will be greatest in precisely those areas where the stolen check supply peaks each month. The Immigration and Naturalization Service's experience with an explosion of counterfeit "Green Cards" since immigration legislation was passed several years ago is not comforting.

There are other components to this underlying problem not completely addressed by S.906. For example, bank locations are not widely available in inner city areas, so convenience and travel costs are factors to consider. In addition, persons who cash a check and convert the entire proceeds to cash are vulnerable to a crushing loss if they are robbed. Finally, the price of forgery is high. Last year we reclaimed $68 million from banks and businesses because they had honored Government checks with forged or improper endorsements. Businesses, including check cashing establishments, have two choices: either "eat" the losses or "self-insure" themselves by spreading the costs over their customer base by increasing fees. Banks will undoubtedly do the same.

Clearly we do not believe that continuing the public's dependence on checks -- even with the introduction of a special identification card -- will produce a safe secure, reliable, effective and relatively inexpensive solution to the problem highlighted by S.906. We do feel, however, there are some other options worth the committee's consideration.

For some time the Financial Management Service has been interested in developing a payment delivery mechanism for "unbanked" benefit recipients which would incorporate most if not all of the advantages which Direct Deposit recipients enjoy. For example, a check recipient's chances of experiencing a lost, stolen or seriously delayed payment are approximately 1500 % greater than those of a recipient receiving an Electronic Funds Transfer (EFT) payment.

Even more important, when a Direct Deposit is misrouted or misposted, which happens occasionally, the problem is usually identified and corrected within 24-48 hours. Processing a check claim, on the other hand, requires from 3 weeks to 3 months to resolve. If a Secret Service field investigation is required to determine whether fraud or forgery has been committed in certain complex cases, the 3 month time frame can, of course, easily be exceeded.

There are other benefits for Direct Deposit recipients. By agreement, financial institutions are required to make EFT benefit and salary payments available for use at the opening of business on the actual payment date, thus assuring timely access to funds. In contrast, a study done several years ago by the Federal Reserve Board revealed that, on an average, 4 1/2 days of float were associated with Social Security check payments. Well over half of the costs of that float were borne by the check recipients.

In summary, electronic payment techniques such as Direct Deposit provide a far higher level of service in the areas of security, dependability, convenience and early access to funds than do check payment. In addition, EFT benefit payments cost the Government only a small fraction of the paper check price tag. So recipients win and the Government wins; the only losers are those people who are in the business of stealing and forging Government checks.

We believe there is a way to provide "unbanked" benefit recipients with an electronic alternative to check delivery even though they do not have a conventional savings or checking account relationship with a financial institution. We plan to test such a technique in a joint experiment with the Social Security Administration starting later this year. One thousand volunteers will be solicited from the ranks of "unbanked" SSI recipients living in three center-city Zip Codes in Baltimore, MD.

"Electronic accounts", which do not require check writing, check reconciliation or account balancing actions by the participants, will be established in their names at a financial institution. Monthly deposits to those accounts will be made electronically by the Financial Management Service. Each participant will receive a plastic access card, which we call a Secure Card", and a personal identification number (PIN). Using the card and the PIN, they will be able to access their accounts and withdraw all or some of the funds credited to the accounts. Access can be made through either automatic teller machines (ATM) or point of sale (POS) terminals in stores in their area.

Participants will not be required to record transactions, track withdrawals, balance checkbooks or live in dread of an overdrawn account and returned check charges. The system will keep the accounting straight and provide account status information upon request.

If this test is successful, it will provide assurance that electronic technology can be used to eliminate both lost, stolen and forged check problems as well as high check cashing fees for the "unbanked". It will also do something else which I believe this committee would welcome: it could offer a variation of "lifeline banking" with many of the benefits of that concept but without many of the problems which currently cause concern in the financial community.

If banks are given the flexibility of selecting either mandatory check cashing services or the electronic "letter of credit" account I have outlined earlier, they may be more receptive to the legislation you are considering. I do not, of course, speak for the banking community in this regard; only its representatives can do that. I can, however, tell you that a solution which increases the quality of service to benefit recipients at the same time it reduces the cost to taxpayers is a good deal for everyone.

Mr. Chairman, thank you for the opportunity to discuss this important subject with the Committee.

Senator DIXON. Very interesting, Mr. Douglas, and we will have a lot of questions of you as well because I think both you and Mr. Brown have some kind of a background of experience here that can be very valuable to us in understanding this subject matter and how it works in fact in the marketplace, and that's important.

Mr. Gagerman.

STATEMENT OF JEROME S. GAGERMAN, PRESIDENT, NATIONAL CHECK CASHERS ASSOCIATION

Mr. GAGERMAN. Good morning, Mr. Chairman and members of the committee. My name is Jerome Gagerman. I am president of Financial Clearings, Inc., of Chicago, IL; chairman of the board of the Community Currency Exchange Association of Illinois; president of the National Check Cashers Association; and chairman of its executive committee.

We are aware that a portion of the population looks with considerable disfavor upon our industry. I submit to you that we are small businessmen trying to make an honest living. Our industry, like any other industry, has members whom we would all consider disreputable. Each of us views with horror the highly publicized instances of customer abuse. Unfortunately, little is mentioned of the fine, reasonably priced services that most of us provide. There are millions of transactions daily in our industry. Of course there are some problems. But I ask you to keep these in perspective.

Our association with over 1,300 locations in 24 States was created with several goals in mind. First, we hoped to create a proper public awareness of our industry. The question has often been asked, "How can they charge for these services? My bank does this for free." The fact is, these services are not free. Traditional financial institutions require minimum balances or levy other charges before any banking services are provided. It must be kept in mind that banks primarily make a profit by lending money. Their other services are designed to attract deposits. When people cash checks at other businesses such as grocery or liquor stores, costs of these services are hidden in the price of the merchandise sold. Our service fees are right up front for everyone to see.

CODE OF CONDUCT

Our second goal has been to establish codes of conduct which would serve to provide guidelines and ethics to better serve and protect the public from abuse.

Our association estimates that there are between 3,000 and 5,000 professional check cashers around the country. Individuals who cannot or choose not to use banks to cash their checks use our facilities, liquor stores, supermarkets or convenience stores. Except for ours, none of these businesses are in the business of cashing checks.

Remember, no check is as "good as gold." A $100 check is not of the same value as $100 in cash. It is only a promise to pay. There are costs involved in converting this promise into cash. This, like any financial transaction, is never free.

Our convenient neighborhood facilities are often in less attractive areas which require special security. In addition, we offer many other services, money orders, notary public service, electronic money transfers, utility payments, credit card cash advances, travelers checks, welfare and food stamp distribution, auto title and licenses, transit tokens and passes, postage stamps and public housing rent acceptance. We provide full financial services.

Many customers use our services for the same reason they go to 7-Eleven or McDonalds—for convenience. The customer is making the same type of choice as patronizing the convenience store instead of the large supermarket.

Unlike other financial institutions, check cashers advance their own funds. They do not have any float to make money. They put their money into the business bank accounts to hold down interest costs. Check cashers risk their own capital and credit by becoming endorsers and guarantors on all of the checks which they cash. Check cashers assume the risks for their customers.

S. 906, while appearing to affect only depository institutions, also has a strong potential for negative impact on our industry. At some of our locations, up to 90 percent of all checks cashed are government checks of one kind or another. The loss of business would force some of our members out of business with the result that check cashing and other services would no longer be available to these consumers.

It is not my purpose to discuss here the cost for specific services. Rather, it should be noted that there are costs involved in providing any services, be these services legal, medical, business or financial. Why can we make a profit at reasonable fees? Our businesses are high volume, low margin, and are located in low overhead buildings. We don't have marble floors or piped-in elevator music and we don't have three floors of vice presidents to pay.

I know you are wondering why we are arguing against S. 906 when cashing government checks exposes us to considerable risk. We have recognized the consumer need and are able to serve it best. We thoroughly understand our risk as a result of experience and the volume of checks offsets losses for the most part. In addition, our customers purchase our other services.

The bill purports to be helpful to the consumer but carefully examine the unintended consequences. This legislation by potentially removing some of our businesses challenges the economic underpinning of an existing industry that is serving thousands of consumers at reasonable fair prices. Enactment of this bill would jeopardize the economic balance by artificially creating new markets that you hope will solve the perceived unsubstantiated problem. People who regularly patronize us won't go to banks when we close due to loss of business. They will revert back to the grocery, convenience, liquor store or bar where their costs will be higher because they are tied to merchandise sales.

Forcing banks to cash checks and removing some of our business—and in some cases, 90 percent of our business—will not change the check-cashing habits of the consumer.

We join with you in an effort to deal with excessive and exorbitant rates, but please do not tamper with an existing system that works. For each person you can show us that was charged an excessive fee, we can show you a thousand times that many who were not.

The GAO has not been able to substantiate consumer problems. Please do not assume massive problems based on anecdotal data. Be sure of the nature and extent of the problem before you attempt to solve it. Please do not attempt to assume a regulatory fix will make the market situation better.

ALTERNATE MEANS OF BENEFIT DISTRIBUTION

The GAO further suggested that Congress should consider alternative means of benefits distribution. I agree that alternative forms of delivery are the best method. We have many friends and supporters in government. In Illinois, our industry distributes monthly to approximately 450,000 food stamp households and 250,000 cases receiving public aid warrants. They may cash their checks with us, which many of them do, or they may go elsewhere. Check distribution in Illinois is free to both the State and the recipient and we indemnify the State and recipient against losses.

We provide a similar service in New York City where we are at the heart of the electronic distribution system. Los Angeles County is currently running a pilot program based on the Illinois model. Much of what we do in Illinois is completely free to both the public and the State. In many other States and cities, our members are integral to the benefit distribution programs.

As a result of our participation, State agencies tell us they have been able to save substantial sums of money due to reduced distribution costs and reductions in fraud. The Illinois Department of Public Aid has written to me, "The system to date is void of losses and provides accountability at each phase of benefit delivery."

I ask that before you recommend legislation, which I don't really believe will solve the perceived problem, you look into other alternative successful means of helping the consumer. Talk to Illinois. Talk to New York City. Interview welfare recipients who receive their benefits from these alternative systems.

Thank you for the opportunity to appear today. We are ready to help you in any way we can to ensure that all consumers have fair service at a fair price. Please do not hesitate to call upon us.

[The complete prepared statement of Jerome S. Gagerman follows:]

NATIONAL CHECK CASHERS ASSOCIATION

Statement

Before the

Subcommittee on Consumer and Regulatory Affairs

of the

United States Senate Banking Committee

Presented by

Jerome S. Gagerman, President

National Check Cashers Association

June 6, 1989

Summary of National Check Cashers Association Testimony

- Significant portion of the population looks with disfavor upon professional check cashers.
    - We are regular, normal small business people trying to make an honest living.
    - We are aware that our industry, like any other, has disreputable members.
    - There is little mention of the reasonably priced services that a majority of us provide.
    - Instances of abuse should be kept in perspective.
- National Check Cashers Association (NaCCA) formed in July, 1987.
    - More than 500 state, corporate and individual members nationwide.
    - Members operating over 1300 locations in 24 states.
    - Illinois has largest concentration of members - over 600.
    - New York second largest concentration of members - over 280.
- NaCCA formed with several goals in mind.
    - Create a proper public awareness of our industry.
    - Establish codes of conduct which provide guidelines and ethical considerations.
    - Hope that combination of public awareness and peer pressure would insure that check cashers engaged in unethical practices would be forced out of business.
- Individuals who cannot or choose not to use banks cash their checks at:
    - Professional check cashers - Clearly posted fees
    - Supermarkets - Hidden in cost of product
    - Liquor stores - Hidden in cost of product
    - Convenience stores - Hidden in cost of product
- Banks are in the business of making loans, not cashing checks.
    - No check is as "good as gold". A $100.00 check is not of the same value as $100.00 in cash.
    - There are costs involved in converting the promise to pay into cash.
    - These transactions are never free.
- Professional check cashers offer full financial services:
    - Money orders
    - Notary publics
    - Electronic money transfers
    - Utility payments
    - Credit card cash advances
    - Travelers' checks
    - welfare payments
    - food stamps
    - automobile license plates
    - auto title registrations
    - public transit tokens and passes
    - postage stamps

  - local housing authority rent payments

- Many of our customers use us for convenience; the same reason they go to 7-11 or McDonald's.

- Unlike banks and other financial institutions, check cashers cannot use their float to make money.
  - Money is placed into their business banking accounts to hold down interest costs.
  - They risk their own capital and credit by becoming endorsers and guarantors.
  - They use their own capital resources to secure relationships with depositories.
  - They assume the risk for their customers.

- Not all fees are dictated by the *marketplace.*
  - Range from a low of .090% to effective high of 1.55%
  - Rates are currently regulated in NY, NJ, IL.
  - Legislation pending in PA, OH, MN, CT.
  - States studying check cashing rates in VA, MD.
  - Legislation has been considered in GA, CA, WA.

- Any rate regulation must take place at the local level.
  - Costs of doing business and staying in business vary significantly from city to city and neighborhood to neighborhood.
  - Local demographics and costs must be examined such as rent, insurance and bank charges.

- In many instances, government checks are the most costly to cash.
  - Risk factors are greater.
    - Fraud
    - Lost and stolen checks

- Often takes years to recoup money from the federal government, and sometimes the check casher must simply bear the loss.
  - Each time a federal check is cashed, check casher faces an 18 month liability for a charge back, even when it can be proved that the check was negotiated for the proper party.
  - Federal government will debit check casher's account for interest after 90 days from reclamation request.

  - Check casher may instruct his bank to refuse to pay a false claim of forgery on a non-federal check if he can prove it is not a forgery.

- Professional check cashers understand the risk involved with cashing government checks, and high volumes offset losses for the most part.

- Enactment of S. 906 has the potential for negatively impacting our business and the consumer.
  - 90% of the checks cashed at some of our facilities are government checks.
  - Even a 15% reduction in the number of government checks cashed could be fatal.
  - Closure or cutbacks in services hurts the consumer, reduces jobs and revenue.

- Professional check cashers can make a profit on reasonable fees.
  - Businesses are low margin, high volume.
  - Businesses are located in lower overhead buildings; they don't have marble floors, piped in elevator music or three floors of vice presidents to pay.

- The GAO has not been able to collect sufficient data to accurately measure the scope or severity of the problem.
  - Says that federal banking regulatory officials have low number of complaints.
  - Suggests that Congress should consider alternative methods for delivery of government benefits.

- Please do not assume massive problems and abuses in the check cashing industry based solely on anecdotal data.
  - Be sure of the nature and extent of the problem before attempts are made to solve it.
  - Do not assume that a regulatory fix will make the market situation better.

- The check cashing industry is an alternative system of delivery of government benefits.
  - In Illinois, the industry distributes government benefits monthly to approximately 450,000 food stamp households and 250,000 cases receiving state public aid warrants. Check distribution free to both state and recipient.
  - In New York City, the industry is the heart of the electronic distribution system.
  - Los Angeles County is running a pilot program based on the Illinois model.

Good Morning. Mr. Chairman and members of the committee, my name is Jerome S. Gagerman. I am President of Financial Clearings, Inc., of Chicago, Illinois, Chairman of the Board of the Community Currency Exchange Association of Illinois, and President of the National Check Cashers Association, and Chairman of its Executive Committee.

We appreciate the opportunity to appear before this committee today to provide you with information about the check cashing industry and our organization, the National Check Cashers Association. We thought that if you were going to address the subject of check cashing, you ought to hear from the experts. We will also share our thoughts on S. 906, entitled the "Government Check Cashing Act of 1989".

I am well aware of the fact that a significant portion of the population, probably including members on this committee, look with considerable disfavor upon professional check cashers. I submit to you that we are regular, normal, small business people trying to make an honest living in an extremely competitive and sometimes politically hostile environment. We are well aware of the fact that our industry, like any other industry, has members whom we would all consider disreputable. In addition, each and every one of us views with horror the highly publicized instances of customer abuse. Unfortunately, there is little mentioned of the fine, reasonably priced services that the great majority of us provide. There are millions of transactions daily in our industry. Of course there are some problems. But I ask you to keep these instances of abuse in perspective.

Membership in the National Check Cashers Association presently consists of more than 500 state, corporate, and individual members operating over 1300 locations in 24 states. Illinois, with more than 600 financial service centers, has our largest concentration of members. New York has more than 280 locations and we are adding new members every day.

Our association was created with several goals in mind. First, we hope to create a proper public awareness of our industry. The question has often been asked, "How can they charge for these services? My bank does this for free." The fact is, nothing is provided for free. Traditional financial institutions require minimum balances or levy other charges before any banking services are provided. It must be kept in mind that banks primarily make a profit by lending money. The other services they provide are designed to do nothing more than to attract deposits. When people cash checks at other businesses such as grocery or liquor stores, costs of providing these services are hidden in the price of the merchandise sold. Conversely, our service fees are "right up front" for everyone to see.

Our second goal has been to establish codes of conduct which would serve to provide guidelines and ethics with which all of our members could comply. We feel that peer pressure within the industry would do much to alleviate the relatively few but highly publicized instances of public abuse. Along with peer pressure provided from within our industry, increased public awareness would insure that the check casher engaging in unethical practices such as overcharging would soon be out of business.

Today, our association estimates that there are between three and five thousand check cashing outlets around the country. Individuals who cannot or choose not to use banks for one reason or another to cash their checks, use our facilities. liquor stores, supermarkets, or convenience stores. Except for ours, none of these businesses are in the business of cashing checks. In the days before banking deregulation (1981), a bank cashed its

customers' checks merely as a service.

Banks are in the business of receiving funds for deposit and making loans. Remember, no check is as "good as gold". A $100.00 dollar check of any kind is not of the same value as $100.00 in cash. It is only a note, a promise to pay when the check is presented to the maker's bank. Consequently there are costs involved in converting this promise to pay into cash. This transaction is never free.

Since the depression, professional check cashing facilities have become increasingly more important delivery points for financial services. Low and middle income consumers and others who cannot maintain the minimum balances required by banks, or choose not to use banks come to us for vital financial services.

We operate convenient neighborhood facilities. They are often in less attractive areas which require special security, and I might add where many banks fear to tread. In addition to cashing checks we offer a wide variety of other services as well. Our member companies offer money orders, provide notary public services, arrange electronic money transfers, accept utility payments, provide credit card cash advances, issue travelers' checks, distribute welfare payments and food stamps, distribute automobile license plates and auto title registrations, sell public transit tokens and passes, sell postage stamps, and collect local housing authority rent payments. We provide, as you can see, full financial services.

But banking deregulation and higher service fees, coupled with branch closings, are just two of the reasons for the proliferation of the check cashing industry. Many of our customers use our services for the same reason they go to the 7-11 or McDonald's. They use our services because they don't want to be inconvenienced by having to park two blocks away or wait in long lines at a teller window, or to arrive at the bank only to discover that the bank is closed. Just like the consumer chooses to pay a little more for a loaf of bread or a carton of milk at a convenience store, the consumer can choose faster more convenient financial services on their time schedules at our facilities. The consumer is making the same type of choice as patronizing the convenience store instead of a large supermarket.

Unlike banks and other financial institutions, check cashers advance their own good funds. They do not have, nor can they take advantage of any float to make money. They put their money into their business bank accounts to hold down interest costs. Check cashers risk their own capital and credit by becoming endorsers and guarantors on all of the checks which they cash. They use their own capital resources to secure relationships with depository institutions. Check cashers assume the risks for their customers.

In both our By-Laws and Statement of Policy, we state that one of our purposes is "To promote and maintain standards of fair and efficient practice in the check cashing industry with a view to promoting the common welfare of its members". We know that in order to stay in business, and to remain competitive, we must offer a good service for fair and equitable fees.

Not all of our fees are dictated by the marketplace. Our fees are regulated in several states, ranging from a low of .090% to an effective high of 1.55%. Rates are currently regulated in New York, New Jersey, and Illinois. In several unregulated states, Texas and Colorado for example, the prevailing rate is less than 2.0%. Pennsylvania, Ohio, Minnesota, and Connecticut have legislation pending that would regulate rates. Virginia and Maryland have passed legislation to study check cashing, and Georgia, California and Washington have considered legislation that would establish rates.

Our association does not have a policy position on the regulation of rates. Some members are strongly in favor of the free market establishing rates, others are operating successfully in states where rates are regulated. It must be stressed however, that when regulation of any check cashing rates are considered, this regulation must take place at the local level. The necessity of regulation only at the local level stems from the fact that the costs of doing business and staying in business often vary significantly, even from neighborhood to neighborhood within the same city. What may be a reasonable rate for Chicago, Illinois, may not be for Los Angeles, California, or Austin, Texas. Los Angeles rates may not be reasonable for Sacramento.

In your letter to the association inviting us to appear today, we were asked to address whether or not low income people pay too much to cash their checks. I have no way of knowing what amount is too much. Local demographics and costs such as rent, insurance and bank charges would first have to be examined.

Another reason we established the organization was to monitor state and federal legislation that might adversely affect our ability to do business. We believe we offer a valuable service to the community which provides an income not only to our families, but to those of our employees, and the many business people who serve us.

S. 906, while appearing to affect only depository institutions, also has a strong potential for negative impact on our industry. Upwards of 30% of the checks our members cash are government checks of various kinds. In fact, at some of our locations, up to 90% of all checks cashed are government checks. The loss of business, particularly in areas where there are large government installations, would force some of our members out of business, with the result that check cashing and the other services we provide would no longer be available to the consumer.

This committee has been charged with investigating rate regulation, specifically for government checks. It must be stressed however, that in many instances, government checks are the most costly to cash. Why? Because the risk factors are greater. A significant expense when cashing government checks is related to check fraud. Most local, state and federal government checks are sent via U.S. Mail, which provides great potential for check

loss and more particularly, stolen checks.

It is not my purpose to discuss here the cost for specific services. Rather, it should be noted that there are costs involved in providing any services; be these services medical, business or financial.

Let me present a very simple example of increased expense involving the encashment of a federal check. In checking her records, A feels she did not get her March social security check on time. She then files a recoupment form with the federal government. In fact, she really did get her March check, but has confused it with a different check. A gets a replacement check for March and cashes that one as well. The check cashing agency which actually cashed her March social security check will be debited by the Social Security Administration even when the check casher can prove that he did cash the check for the proper party. It often takes years to recoup this money from the federal government and quite often the check casher must simply bear the loss. Every time I cash a federal check I face at least an eighteen month liability for a charge back on that item; even when I can prove that the check was negotiated for the proper party.

On the other hand, if I cash a non-federal check which is returned to me as an alleged forgery, I may instruct my bank not to pay it so long as I can prove that it is indeed a false claim of forgery. I cannot do this with federal checks because the federal government will start debiting my account for interest after 90 days from the date of request for reclamation. I can provide you with many more examples of higher costs, particularly when dealing with federal checks.

I know what you are thinking. Why is this man arguing against S. 906 when cashing government checks exposes him to such risk? We have recognized the consumer need and taken steps to serve it. Furthermore, we thoroughly understand our risk as a result of experience, and the volume of checks offsets losses for the most part. In addition, our customers generally purchase other services we offer at our facilities.

I am not here today to support the banking industry, it is quite capable of doing that itself. I am, however, going to tell you that if you enact this legislation, you may severely injure our business; many of our members will not be able to maintain the level of services they currently offer. In addition, the loss of government check cashing in some cases may result in closure of facilities, reduced hours and employee layoffs. Our businesses are low margin. Low margin requires high volume. Even a 15% cutback on the number of government checks cashed could be fatal.

If enacted, this legislation will force banks to enter a business they never wanted to be in in the first place. As I said a few minutes ago, banks are not in the business of cashing checks. They make loans upon which people pay interest. They don't want to cash checks, and they don't do it very well. They don't know how to recoup their costs like we do, because we have been doing it for years as our principal business. In effect, by the time banks truly realize the costs involved in cashing checks of any kind and these costs are passed on to its customers, the charges will generally be higher than the service fees most of us are presently charging. Meanwhile, during this learning process, many of our members will be forced out of business.

And what happens to the consumer? The bill purports to be helpful to the consumer, but carefully examine the unintended consequences. When some of our outlets are forced to close, especially in areas where there are no banks, the neighborhood has lost a valuable service, jobs, and revenue. You can't force the bank to like cashing checks and their service will inevitably reveal that.

Why do I sit here and tell you that we can cash checks and make a profit for reasonable fees, and regulated fees in some states, and the banks can't possibly break even on fees lower than ours? Because our businesses are high volume, low margin and are located in lower overhead buildings; they don't have marble floors or piped in elevator music, and they don't have three floors of vice presidents to pay.

The GAO in its October, 1988 report stated that: "There are not sufficient data to accurately measure the scope or severity of problems individuals without banking accounts are experiencing cashing government checks... While consumer advocacy groups and others believe that many low- and moderate-income consumers have difficulty cashing government checks, nationwide statistically valid data on the extent or cause of difficulties are unavailable". The GAO asked the federal banking regulatory agency officials if their complaint handling systems had received complaints from individuals experiencing check cashing problems. In all cases, they said complaints had been low. Please do not assume massive problems based on anecdotal data. Be sure of the nature and extent of the problem before you attempt to solve it. Please do not assume that a regulatory fix will make the market situation better.

The GAO further suggested that if Congress determines that recipients of government checks should not bear the costs of cashing them, or should be assured of a low-cost option, it should consider encouraging other methods: "Requiring banking institutions to cash nondepositor checks is not the only way to improve individuals' access to government benefits". I agree that alternative forms of delivery are the best method.

We have many friends and supporters in government. In my home state of Illinois, our industry distributes monthly to approximately 450,000 food stamp households and 250,000 cases receiving state public aid warrants. Recipients produce identification, and we present them with their check, or food stamps. They may cash their check with us, which many of them do, or they may take it and cash it elsewhere. Check distribution in Illinois is free to both the state and recipient. At the same time we indemnify the state and the recipient against losses.

We also provide a similar service in New York City. In fact, we are the heart of the electronic distribution system. Los Angeles County is currently running a pilot program based on the Illinois model. Much of what we do in Illinois is completely free to both the public and the state.

We have letters from the state agencies telling us how much money they have been able to save as a result of reduced distribution costs and reductions in fraud. The supervisor of the procurement management section of the Illinois Department of Public Aid has written to me in a letter that "The system to date is void of loses [sic] and provides accountability at each phase of benefit delivery."

Mr. Chairman, I ask that before you recommend legislation, which I don't believe will really solve the perceived problem, that you look into other alternative, successful means of helping the consumer. Talk to the state of Illinois, or the city of New York. Interview some welfare recipients who receive their checks from these alternate systems.

Thank you for the opportunity to appear today. We are ready to help in any way we can to ensure that all consumers have fair service at a fair price. Please do not hesitate to call upon us.

Jerome S. Gagerman
President, National Check Cashers Association

Senator DIXON. Thank you, Mr. Gagerman. Your testimony is very interesting and I'm sure we'll have quite a few questions for you.

Rosemary Dunlap is the Secretary of the Virginia Citizens Consumer Council. We are delighted to have you here.

STATEMENT OF ROSEMARY DUNLAP, VIRGINIA CITIZENS CONSUMER COUNCIL

Ms. DUNLAP. Good morning, Mr. Chairman. Good morning, Senator Bryan and Senator Metzenbaum. Thank you for the opportunity to testify.

VCCC is a statewide consumer advocacy organization. For over 20 years our members have supported proconsumer legislation before the Virginia General Assembly, represented consumers before State regulatory agencies, and worked to inform our members and the public on consumer issues.

We appreciate this opportunity to speak in support of Senator Metzenbaum's legislative proposals to improve access to affordable banking services for low and moderate income consumers. S. 906 and S. 907, when enacted, will require banks to cash government checks for nondepositors at cost and to offer low-cost basic checking accounts at cost. They will help close the widening gap between those consumers with the least resources and the bank services necessary to safely and economically conduct the simplest financial transactions.

Access to basic banking services has been a high priority for VCCC for the last few years. We published a Consumers Guide to Banking Services in Virginia in 1986 to help consumers shop for the best accounts. We participated in the 1988 CFA annual bank fee survey. We published a study of nonbank check-cashing businesses in Virginia early this year. VCCC's latest legislative agenda included basic banking proposals in 1988 and 1989.

We are proud to report that the 1989 session of the Virginia General Assembly unanimously adopted Senate Joint Resolution 226, patroned by Senator Robert Scott of Newport News. The resolution establishes a study committee of legislators to examine four issues and to report its findings and recommendations to the 1990 session. The issues to be studied through public hearings and expert testimony are: (1) the availability of low-cost checking accounts, (2) bank policies on cashing government checks for nondepositors, (3) the identification needed to prevent fraud, and (4) the fees and practices of nonbank check-cashing outlets.

I've brought for the members a copy of the resolution.

Since it is widely known that Virginia is not a hotbed of radical consumer activism, you might reasonably wonder why the affordable banking issue has moved to the front burner of legislative attention. As a result of VCCC's work on these issues, we were able to point out these developments that we hope will help you in your consideration of congressional legislation.

Very few banks voluntarily offer and widely publicize low-cost basic checking accounts. In our April 1988 survey, of the ten largest banks and thrifts in Virginia, we found only one bank that offered what we would define as a lifeline checking account. At Central Fidelity, you can have a noninterest-bearing checking account with 12 checks per month for $3. By contrast, another bank has been conducting a heavy advertising campaign to offer consumers free checking accounts and seven other free services; but it is only available to consumers who have $10,000 on deposit or who borrow $10,000 from Dominion Bank.

The cost of using bank services for all consumers is going up faster than the rate of inflation nationally according to CFA's annual bank fee surveys. When we compared Virginia averages with CFA's national findings, we found that Virginia banks charge more in monthly fees for noninterest-bearing checking accounts—$5.33 per month in Virginia, $4.40 nationally.

We cited the General Accounting Office report finding that 75 percent of families receiving Aid to Families with Dependent Children, 50 percent of people on Supplemental Security Income, and 14 percent of Social Security recipients do not have checking accounts.

The majority of Virginia banks do not cash even government checks for noncustomers. In our 1988 Bank Fee Survey, eight of the ten banks surveyed responded that they do not cash these checks. A later telephone survey of all the banks listed in the Newport News C&P Yellow Pages found that one-third would cash only certain checks for some people under limited circumstances.

The real attention-grabber was the study of nonbank check-cashers. This unregulated service has emerged in the last three years mainly in the urban areas of Virginia—Richmond and the cities in the Tidewater area. VCCC contacted seven check-cashing companies with twenty outlets. Among our findings: Virginia check-cashing outlets charge an average of $11.65 to cash a $320 computer printed payroll check for a person with good identification; charges for cashing a $500 Social Security check with identification ranged from $7 to $15; the average first-time cost of cashing a $369 AFDC check was $12.87; and check-cashing fees in Virginia are twice the national average found in a similar 1987 CFA study. Virginia charges are three times the rate charged in New York where fees are regulated.

Senator DIXON. Ms. Dunlap, could you clarify for me where you're getting these numbers from? I hear all your numbers. Whose numbers are those?

Ms. DUNLAP. Those are from our survey.

Senator DIXON. Your survey?

Ms. DUNLAP. Yes.

Senator DIXON. OK.

Ms. DUNLAP. A copy of our full report is available.

VCCC urges the Congress to enact S. 906 to require banks to cash government checks for nondepositors and S. 907 to mandate low-cost basic checking accounts. We believe that banks have an obligation to serve the financial needs of the whole community, not just the most affluent. We need to make sure that low and moderate income consumers are not being excluded from the safety and convenience of using banks either by neglect or deliberately. These two bills strike a fair balance between the wishes of consumer representatives and the banking industry.

Thank you.

[The complete prepared statement of Rosemary Dunlap follows:]

Virginia Citizens Consumer Council
1611 S. Walter Reed Drive • Arlington, Virginia 22204
703-892-0330

VIRGINIA SURVEY OF CHECK CASHING OUTLETS

Virginia Citizens Consumer Council
January, 1989

Background

Non-bank check cashing businesses have emerged in Virginia as a new form of financial services during the last two or three years. A market for their services is growing in the urban areas of Richmond and the Tidewater as the cost of bank checking accounts have grown and banking services have become less available to moderate and low-income consumers. The majority of banks in Virginia will not cash government benefit checks for non-depositors. Those few that do cash a limited range of checks charge from $3 to $5.

Check cashing outlets are not regulated by state government in Virginia. Therefore, no standards exist for fees charged or the disclosure of fee information.

Survey

The Virginia Citizens Consumer Council surveyed seven non-bank check cashing companies with 20 locations in Richmond, Newport News, Hampton, Norfolk, Virginia Beach, Chesapeake and Portsmouth. The survey was conducted by phone during January, 1989. On-site visits were made to several offices during November, 1988.

The survey design parallels a national survey conducted by the Consumer Federation of America in September, 1987, so that data from Virginia can be compared with national averages. The VCCC averages are weighted based on the number of outlets per company. Where two sets of figures are shown, they reflect the outlets' practice of charging a higher fee for the first time customer and a lower fee for repeat cashing of the same type of check.

We surveyed the charges for cashing a payroll check, a Social Security check, an Aid For Families With Dependent Children check, and a personal check. We also asked the cost of purchasing a $50 money order. Surveyors noted fee disclosures at the outlets and asked if fees are quoted by phone to customers.

Results

The cost of using a check cashing outlet varies widely. Charges for cashing a computerized payroll check for a person with picture identification ranged from 1.5 percent to 4 percent for a first time customer and 3 percent for a repeat customer. Charges for cashing a Social Security check ranged from 1.4 percent to 3 percent/2 percent. Charges for cashing an AFDC check ranged from 1.4 percent to 4 percent/3 percent. The two companies that cash personal checks charge 10 percent of the face value of the check.

Virginia check cashers calculate their fees on a fixed percentage of the value of the check, although a few outlets quoted the dollar amount. Two companies charge a higher fee for first time customers and lower rates for subsequent checks of the same kind. Two companies charge an additional 2+percentage points if the customer does not have identification. For example, Anykind Check Cashing in Richmond charges 6 percent to cash a Social Security check without identification and 3 percent if the person has identification. Almost A Banc adds a flat 2 points above the fee schedule for lack of identification.

Payroll Check

We asked for the charge for cashing a computer written payroll check of $320. Charges ranged from $4.95 to $12.80/$9.60. The average charge was $11.65 for a first visit and $8.99 for repeat customers. Handwritten payroll checks cost more to cash at Almost A Banc in Tidewater (6 percent/4 percent.) By comparison the average cost of cashing a $320 payroll check in the national CFA survey was $5.31.

Government Checks

Each company was asked what they would charge to cash a $500 Social Security check and a $369 AFDC check for a person with identification. Only Almost A Banc made a fee distinction between the two types of checks. Charges for cashing a $500 Social Security check ranged from a low of $7 to a high of $15/$10. The average charge for a $500 Social Security check was $13.84/$9.67. The average charge for a $369 AFDC check was $12.87/$10.25. The CFA average for the $500 Social Security check was $8.47 in 1987.

Personal Checks

Personal checks are more risky to cash so it is not surprising that only two surveyed companies cash this type of check. For a $150 personal check, both companies charge $15 or 10 percent. The national average was $6.77 in 1987.

Other Fees

Check cashers handle a variety of financial instruments with a range of fees. For example, Anykind Check Cashers charges 6 percent/3 percent to cash insurance drafts and checks, 6 percent for cashiers checks, 10 percent to cash money orders and travelers checks and 6 percent to cash federal and state tax refunds.

Money Orders

Most check cashers also sell money orders. For a $50 face value money order, Virginia outlets charged from 25¢ to 49¢ for their regular check cashing customers. By comparison the U. S. Post Office charges $1 for a $50 money order. All outlets charged a flat fee for money orders.

Outlets Refusing to Give Information

Two Virginia companies refused to quote fee information to surveyors. One of these, Dominion Check Cashing in Newport News also did not post fee information at their place of business. Only one company surveyed stated that they routinely quote fees to consumers who call to inquire. The majority state that it is company policy not to quote fees over the phone. Fee information is not posted prominently in those outlets visited, but is usually a type-written list posted on the tellers' windows.

Differences Within Cities

The range of rates for the same type of check within the same city is striking. In Richmond, a $320 payroll check can cost from $4.95 to $9.60 to cash for a repeat customer. In Newport News, a first time AFDC $369 recipient can pay from $7.38 to $14.76.

Total Annual Costs

Consumers who rely exclusively on check cashing services for financial transactions can pay a staggering price. A worker who cashes fifty $320 payroll checks a year and who buys six money orders a month could pay as much as $518.48 at Anykind Check Cashing in Richmond or $501.20 a year at Almost A Banc in Tidewater or as little as $272.70 at Richmond Check Cashers.

The annual cost to a Social Security recipient who cashes twelve benefit checks a year and buys four money orders each month ranges from $158.52 at Anykind Check Cashers and $137 at Almost A Banc to $101.40 at Richmond Check Cashers.

For those consumers who have access to a bank or savings and loan, opening a checking account is less costly than relying exclusively on check cashers. A 1988 VCCC survey of ten banks and thrifts in Virginia indicate that maintaining a non-interest bearing checking account where available is less costly than using a check casher to handle payroll checks and money orders. Social Security recipients are better off at banks and other depository institutions that offer free or special accounts to senior citizens.

The majority of banks in Virginia will not cash government checks for nondepositors, based on VCCC surveys. Those that do cash checks on a selective basis charge from $3 to $5 for the service. Basic checking accounts that are affordable to low-income consumers are not uniformly available around the state. Not all consumers are able to maintain a relationship with a bank that permits free check cashing. Factors that interfere include high mobility, the lack of math and reading skills, distrust or lack of familiarity with banks, and distance to an affordable bank for people with no transportation.

There is a market for nonbank check cashing outlets. VCCC recommends that the General Assembly study their fees and practices to determine if these businesses should be regulated as financial service companies by the State Corporation Commission.

Regulation of Check Cashing Services

Four states currently regulate non-bank check cashing businesses: New York, New Jersey, Illinois, and Connecticut. Regulated maximum fees range from 3/4 of 1 percent of the face value of the check plus 10¢ per check in New York and Connecticut to 1 percent for in-state checks and 1½ percent for checks drawn on out-of-state banks in New Jersey. Illinois limits rates to 1.2 percent plus 90¢ per check. These regulated rates are far lower than rates being charged in Virginia, yet there is no shortage of check cashing outlets in those four states. This leads us to believe that rates being charged in Virginia are excessive and unfair to those low-income consumers who must use non-bank check cashers to handle their finances.

Recommendations

VCCC recommends that consumers who have access to checking accounts at banks, savings and loans, or credit unions compare the cost of using those accounts against the cost of paying to cash checks and buy money orders.

If the consumer lacks access to banks, has insufficient identification or resources to use banks, and must rely on commercial check-cashers, VCCC recommends shopping around for the best rates. Rates are not regulated and vary widely.

VCCC urges the General Assembly to enact a study resolution to investigate the availability of low-cost checking accounts, bank policies on cashing government checks for nondepositors, and the rates and practices of check-cashing businesses.

COSTS TO CONSUMERS OF CHECK CASHING SERVICES IN VIRGINIA

Check Cashing Outlet	Payroll Check $320		Social Security $500		AFDC $369		Personal Check $150	Money Order $50
	1st /	Repeat	1st /	Rep.	1st /	Rep.		
• Almost A Banc 13 outlets in Tidewater area	4% $12.80	3% $9.60	3% $15	2% $10	4% $14.76	3% $11.07	10% $15	25¢
• Anykind Check Cashing 2 outlets/Richmond	4% $12.80	3% $9.60	3% $15	2% $10	3% $11.07	2% $7.38	10% $15	49¢
• Quik Check Cashing Richmond	2% $6.40		1.4% $7		1.4% $5.17		NA	NA
• Richmond Check Cashers	1.2% $4.95		1.4% $7.05		1.4% $5.17		NA	35¢
• Virginia Check Cashers Newport News	2% $6.40		2% $10		2% $7.38		NA	40¢
Virginia Average (weighted by no. of outlets)	$11.65/$8.99		$13.84/$9.67		$12.87/$10.25		$15	
CFA National Average 1987	$5.31		$8.47		$6.24		$6.77	
New York Regulated Rate	$2.50		$3.85		$2.87		NA	
• Dominion Check Cashing Newport News	Refused to quote fees. Does not post fees in lobby.							
• National Check Cashing Richmond	Refused to quote fees over the phone.							

Senator DIXON. Thank you very much, Ms. Dunlap. I'm sure we'll have some questions of you. Your testimony is very interesting as well.

Let me observe that two of my distinguished colleagues have joined the panel since the testimony began—the Senator from Nevada, Senator Bryan; and the Senator from Missouri, Senator Bond. Do either of you gentlemen have a statement that you want to make or a statement you want to put in the record before we start the Q and A?

Senator BRYAN. Mr. Chairman, I don't. I'll just defer to the questions.

Senator DIXON. I thank the Senator from Nevada.

The Senator from Missouri.

OPENING REMARKS OF SENATOR BOND

Senator BOND. Thank you, Mr. Chairman.

I am delighted to be here and to have the opportunity to hear the testimony. We've reviewed the statements in advance.

As a former Governor, I am delighted that we are getting the input from State officials. I think the State leadership is very important in these areas and we are most grateful to have you testify before us and I also want to commend our colleague from Ohio, Senator Metzenbaum, for revisions he's made in his check-cashing bill. Some of the objections raised on the earlier legislation have been dealt with and, Chairman Dixon, I certainly look forward to working with you on these issues. I hope we can craft some sensible compromises.

Senator DIXON. I thank the Senator from Missouri.

Ladies and gentlemen, we're going to have a Q and A now. We will limit the question and answer period to 10 minutes per Senator here. Senator Bond, may I say that before you arrived we had agreed that Senator Metzenbaum would participate in the Q and A. I'm sure you have no objection to that.

To start it off, let me say this as the chairman. As I see at least the first issue, the question of the check cashing, you have this broad question. On the one hand you have some, like my friend, Ms. Dunlap, who would say that you ought to cash the checks and so forth at no cost; and I think there are some in the Senate that would say the same.

And on the other side of the coin, I suppose you have some who would say government oughtn't to get into this question at all, it isn't one of our questions, this is a free market question and let the marketplace decide that. I guess those are the parameters of this thing.

Somewhere in the middle I guess some of us would like to know, assuming banks and thrifts and other things are not eleemosynary institutions—and I think they are not—then they operate for a profit. Good for them. That's the American system. If that is the case, then I suppose the question that some of us would like to have answered are, first of all, what is a fair cost for this kind of a service? I would have to say I don't know that and maybe there's no criteria exactly to determine that. Second, I'm sure that you can get insurance—at some point in time I'll talk to Mr. Gagerman about that as to whether currency exchanges and others do that—to insure against losses for cashing checks.

But I thought I'd start with you, Mr. Brown. I take it in Connecticut, from what you said, you first had a bill you couldn't pass and you then entered into some kind of accommodation and I suspect what you ultimately did was you limited the types of checks that could be cashed. You said they were your State checks for AFDC and welfare and things of that kind. The State checks for these purposes, you limited it specifically to certain kinds of checks.

PROFIT FOR CASHING CHECKS

Now then did you let the financial institution make a profit for cashing them?

Mr. Brown. No, Mr. Chairman, we did not. What we attempt to do was to quantify and qualify the various benefits that the State and the municipalities through the depository accounts with the various banks contribute to banks.

Senator Dixon. In other words, you put some State money in the banks and—I was a State treasurer once. I understand this part certainly. Believe it or not, before I was State treasurer—well, in all fairness, my predecessor got interest as well, but there was a time in history when Illinois didn't get interest at all for depositing money in State banks. That was a wonderful arrangement in those days, but obviously we don't do that now and we do get interest. But that's what you're talking about. You said, "Look, we're giving you this and you give us this."

Mr. Brown. Exactly. We looked at some of the benefits that the banks enjoy and we figured that a balance should be struck with a very limited classification of instruments which were those which you just described.

Senator Dixon. Now if I may interrupt in the interest of time, in fact, in Connecticut, if a person comes in with a welfare check for $260 or whatever it is, the bank does not charge at all?

Mr. Brown. That is correct, Mr. Chairman.

Senator Dixon. Now I would suggest that would be a thing that would be perhaps not so acceptable an idea at the Federal level, but that is at least the way you do it in Connecticut.

Mr. Brown. That is the way we do it in Connecticut.

FRAUD AND FORGERY

Senator Dixon. What about the problem of fraud? What about the problem of forgeries and things like that? I got the impression you were saying in Connecticut a person has to do it individually——

Mr. Brown. The payee who is described in the instrument itself. It does not allow for a third party.

Senator Dixon. Alan Dixon comes in and says, "Here's my check and I'm Alan Dixon and here's the card that proves it. Look, I've got the picture on it."

Mr. Brown. Right.

Senator Dixon. Is that right?

Mr. Brown. That's right.

Senator **Dixon**. Was it you that said you need two identification cards in Connecticut?

Mr. **Brown**. You need two identifications which cover three features, a picture, a photograph and a signature.

Senator **Dixon**. A picture, a photograph—what's the distinction?

Mr. **Brown**. I'm sorry. A picture, identifying number and a signature.

Senator **Dixon**. Like your Social Security number. In Illinois, believe it or not, when I was Secretary of State, we started pictures on the driver's license. I love to talk about the things I did when I was there. So obviously you could have your driver's license; that's got the picture on it and here's the signature. What other card do you use?

Mr. **Brown**. The picture, the signature, and the identifying number are the three items.

Senator **Dixon**. But they're on the one card. In Illinois on the driver's license you have the picture, the Social Security number and the signature.

Mr. **Brown**. We would still require another source of identification.

Senator **Dixon**. So what would be the other source?

Mr. **Brown**. The other source could be a credit card. It could be a——

Senator **Dixon**. But there wouldn't be a picture.

Mr. **Brown**. Correct. There would not be a picture. It would take those two sources of identification to come up with those three features.

Senator **Dixon**. OK. It's clarified now. I got the impression for a minute, Mr. Brown, you were suggesting both cards had to have all that stuff on them. You're not saying that?

Mr. **Brown**. No, sir.

Senator **Dixon**. As long as the aggregate of two cards gives you a picture, an identifying number which for most of us is the Social Security number I presume, and a signature, that would do it?

Mr. **Brown**. That's correct.

Senator **Dixon**. Now I've got to think this through a minute because I'm not an expert in the field. But is there still a possibility of fraud and that sort of thing here? I'm trying to think this out a little bit out loud.

Mr. **Brown**. Certainly there's a possibility, but I think it's substantially reduced. As a matter of fact, the criteria established by the statute, those three features, are more than the average bank had required. The bank only required a license with a picture on it, a driver's license, and that would do it.

Senator **Dixon**. Now let me see if I can get this clear with you, Mr. Brown, because frankly in your case you're a guy inside this system, you did something and you've got a result. I take it you're satisfied with the result in Connecticut.

Mr. **Brown**. We are satisfied with the initial legislation.

Senator **Dixon**. Are the bankers satisfied?

Mr. **Brown**. The banking institutions are very satisfied.

Senator **Dixon**. Now what about loss? Is there any loss found yet in the system in Connecticut?

Mr. **Brown**. We have not identified any loss that's unique to welfare recipients that does not permeate the entire society with regard to various classifications of instruments which are being negotiated.

Senator **Dixon**. OK.

Mr. **Brown**. As a matter of fact, there's probably less.

DIRECT DEPOSIT

Senator **Dixon**. Now, Mr. Douglas, you talked about this direct deposit thing. I suspect that's not a thing a lot of average people on the street are going to want to do. I hear what you're saying, but assume for the purposes of our discussion a lot of people don't want to do it.

Now you were talking about $68 million in losses out there for the Federal Government.

Mr. **Douglas**. Not for the Federal Government. For the banks or businesses who accepted a check with a forged or improper endorsement. We reclaim that money for the Federal Government.

Senator **Dixon**. Now I take it, without knowing this but I suspect it to be true, that obviously a great many institutions insure against those kinds of losses.

Mr. **Douglas**. I do not know that. I suspect that where people charge fees that they self-insure themselves, that the fee covers some sort of margin for the losses they would expect to experience. And I guess Mr. Gagerman could give you a better answer on that.

But let me make a point concerning your comment about the popularity of direct deposit. The largest volume of payments we make are to Social Security recipients, the retirement thing. We are at the point now where half of Social Security recipients receive their monthly payments through direct deposits.

Senator **Dixon**. I'm surprised to hear that.

Mr. **Douglas**. For Federal employees salary, the percentage is around 75 percent. Both of those percentages are increasing and have been for a while.

Senator **Dixon**. They identify a bank that will be their depository and you send it directly?

Mr. **Douglas**. A bank or S&L or a credit union.

Senator **Dixon**. I mean a financial institution.

Mr. **Douglas**. Yes, a financial institution.

Senator **Dixon**. That's very interesting.

May I switch from you to Mr. Gagerman for a minute. Of course, we call them currency exchanges. I don't know what they have in other States, but similar types of institutions.

Do they insure against losses for the checks that they cash?

INSURANCE AGAINST LOSS

Mr. **Gagerman**. The insurance that exists for the encashment of bad checks—and we would even have to get into an explanation of what actually constitutes a bad check as opposed to simply a monetary loss—is going to depend upon statute from State to State.

In Illinois, which I think is the most closely regulated when it comes to insurance, there is a kind of insurance called the bonding. In reality, it's nothing more than the payment for certain kinds of bad checks but then the insurance premiums immediately rise to the point where the claims are paid directly back to the bonding company.

I think in the long run, the answer is no, there is no such thing as insurance against the encashment of a check where a monetary loss takes place.

Senator **Dixon**. Well, is that generally true in our society? Are you saying that there's some kind of a standard deductible amount so that you carry some of the loss in your institution but you're insured against the big losses? Is that what you're saying?

Mr. **Gagerman**. Well, there is a deductible as per statute in Illinois. But again, any claims that we make will eventually be reflected in our increased premiums on the bonding which we must carry by statute in Illinois. We will pay it back to the bonding company.

Senator **Dixon**. OK. One quick question, Ms. Dunlap, because my light is yellow. I would just like to clarify this from the perception of the consumer groups because I heard you when you said "no cost" several times.

Are you really saying to us that financial institutions ought to do this at no cost, sell the potatoes at no profit, and so forth? Are you really saying that? Would you have a problem as a consumer group with the kind of a modest cost that protected the financial institution to pay for the actual cost of doing it, with a modest profit, plus somehow insuring against any losses from that added risk in that kind of business?

Ms. **Dunlap**. I believe that we could support doing it at cost.

Senator **Dixon**. Well, I know you'll do it at cost. That isn't the question. So many of us like to work and get paid for it and I was wondering about that.

Ms. **Dunlap**. OK. That's a good question and I'd be glad to have CFA address it because they are a nationwide organization and we're a member organization of CFA.

Senator **Dixon**. This Senator would want to know about that, frankly. I'm not in the business of telling people to do things at cost and I would want to hear—and I want to be open about that—about that part of it.

There are two things I want to stress before I yield the floor and I see the red light on and I ought not begin by making this bad beginning and talking into the red light, but I think you ought to be able to be protected against losses if you're going to do this and there's an added risk in it, and I think you ought to be able to make a little profit because that's what people are in business to do. I thank you, Ms. Dunlap.

If the Senators don't mind, we were going to use the "early bird" rule and I believe since you've already indulged the chair and said that the Senator from Ohio is a participant, and he should be, the Senator from Ohio.

Senator **Metzenbaum**. Mr. Chairman, I appreciate your graciousness, but if the other members of the committee have other commitments and have to get away, I'd be willing to bide my time.

Senator **Dixon**. Why don't you go ahead, Senator Metzenbaum, and I'm going to ask Senator Bryan to chair for a moment. I have to make an important phone call.

Senator **Metzenbaum**. Thank you very much.

Mr. Brown, I appreciate your testimony and I also appreciate what has been done in Connecticut.

Connecticut banks aren't allowed to charge anything. Do you know how much it costs them to actually process or cash these checks?

Mr. **Brown**. We have figures that I'm not really willing to rely on, Senator. We are in the process of eliciting from the banks their actual costs. They will charge anywhere from 17 to 18 cents per item, but they do not represent that those are actual costs. There's no standardized manner in which they arrive at these figures. I'm sorry I don't have a better answer for you.

Senator **Metzenbaum**. I noticed there was a GAO report that was prepared on this question of loss and the GAO said, "As for fraud, we found the actual dollar amount Treasury reclaims—and this is only U.S. Treasury—from banks and thrifts or refused payments to be quite small." Then they go on to point out that under losses on the reclaimed checks, I guess the losses, there were those that they had to go out and find—about $64 million as against $622 billion worth of checks. My mathematics indicate to me that that's about one-tenth of 1 percent. On a $500 check, approximately 50 cents.

As you and others know who have seen this legislative proposal, our bill provides that the banks can charge the cost of cashing the check, including the fraud losses as determined by the Federal Reserve Bank, based upon actual cost studies.

So I'm not here saying banks should have to suffer an economic loss. I'm saying that they ought to be covered by their exposure with respect to fraud or fraudulent checks and also with respect to any incidental costs. I think you indicated something like 17 cents a check or something.

Mr. **Brown**. That includes a profit.

FOES OF DIRECT DEPOSIT

Senator **Metzenbaum**. All right. Now, Mr. Douglas, as you probably know, the AARP will testify later that many senior citizens don't like direct deposits. They've heard complaints that checks get deposited in the wrong account and they've heard about cases where people lose access to their money for months.

Would you care to make any comment on that as to what your actual experience has been?

Mr. **Douglas**. Yes, Senator, thank you.

I am aware that AARP says that they have gotten complaints from their membership about direct deposits and I'm quite sure that's correct. I think it's a matter of proportion.

My point that I made earlier was that if you take 1,000 people or 100,000 people who receive their payments by check, and an equal number who receive them by direct deposit, the group which gets checks are going to be 1500% more likely to be at risk of having either a lost, stolen, and delayed check payment.

When that occurs, it's going to take a long time to straighten out the problem.

Now that does not mean that there aren't problems with direct deposit where a digit is mistaken and it goes into the wrong account or the wrong routing number. But those kinds of mistakes happen very infrequently, particularly in relation to checks, and they can be corrected very, very quickly in relation to solving missing check problems.

Senator Metzenbaum. When you make yo[illegible] direct deposit, how soon after the direct deposit is made can the payee get his or her money out.

Mr. Douglas. That is an excellent question, Senator, because we have an arrangement with financial institutions that the money is available at the opening of the business day on which the payment is due. The money is available to the account holder at the beginning of the business day, even though we do not actually pay the bank for the gross amount involved with direct deposits until later that day through the Federal Reserve settlement system.

One other point. About 4 or 5 years ago, the Federal Reserve did a survey in which they looked at the amount of float time on Social Security checks and the average was 4½ days of float. Now the banks are only eating about a day to a day and a half of that. The rest of it is borne by the Social Security check recipient, which means that, on average, people are not getting the availability of those check funds on their Social Security payments for 3 days on their own. That doesn't include the float that the bank is involved with.

Senator Metzenbaum. How much do you think that float is worth on the checks that you're presently issuing?

Mr. Douglas. I don't have that figure, Senator, but we could get it and provide it for the record because we actually maintain the Social Security trust funds in the Financial Management Service as well as making payments for Social Security. We have an arrangement where we give a credit to the Social Security trust fund for that float.

Senator Metzenbaum. But I'm concerned and I think there's a reason to be concerned about the value of the float to the banks. I remember banks saying it takes 7 days to cash a check. That's one of the absurd things that they've said. We've legislated on that subject and made them give you the money earlier. But frankly, I must confess, I thought holding the checks that long was almost fraudulent.

Mr. Douglas. But I'm not talking about where banks are saying, "Well, I'm going to hold a check longer." I'm saying that this is the float which results in the recipients themselves not getting the availability of that money because they are not getting to the bank quickly to cash or deposit that check.

Senator Metzenbaum. That benefit is redounding to the Federal Treasury.

Mr. Douglas. That's right, but it's on the back of the Social Security recipients, so I'm not sure it's a good tradeoff.

Senator Metzenbaum. Mr. Gagerman, you say most check cashers charge reasonable rates. What would you say is a reasonable rate?

Mr. Gagerman. I've been expecting that question, Senator. I think before I could even answer that—and I'm not purposely trying to be vague—it must be recognized that there are different cost factors for many different kinds of checks and before I could even begin to address what is specifically called a reasonable rate figure, there would have to be studies not only in areas of the country but literally in particular different neighborhoods, which is something our own banking department has done simply because the cost of doing business and the cost of staying in business vary so significantly even from neighborhood to neighborhood within the same city.

Senator **METZENBAUM**. But overall, on a general basis, what would you think is a reasonable rate? One percent, 2 percent, 5 percent?

Mr. **GAGERMAN**. I don't even have those kind of statistics available.

Senator **METZENBAUM**. Are you aware of the fact that only three States regulate check cashers, Illinois, New York, and New Jersey?

Mr. **GAGERMAN**. That was in my presentation. Yes, sir, I am.

Senator **METZENBAUM**. The regulators in New Jersey found overcharges at every check cashing outlet they examined. Now maybe Illinois is doing OK, but it's clear that there are problems in New Jersey and it's clear from the testimony of this lady, Rosemary Dunlap, that there are problems in Virginia.

Frankly, Mr. Gagerman, I think you're in a legitimate business and I think you speak for a legitimate industry. But tell us how to solve the problem without passing Federal legislation.

SOLVING THE PROBLEM WITHOUT FEDERAL LEGISLATION

Mr. **GAGERMAN**. I think it is absolutely critical—and I have said this many times before—that when these issues do become a problem there are two aspects involved. One is local legislation and it must be done only on the local level, primarily because of the variances in cost. The other obviously is enforcement. I can't relate to enforcement. I can definitely relate to local regulation.

It would be the same as saying what does an attorney in New York City or on Wall Street has as his hourly rate as opposed to someone from Ames, IA; is he having a lower hourly rate? It's got to be tied into market conditions.

Senator **METZENBAUM**. Ms. Dunlap, you have some pretty alarming numbers on the rates check-cashing outlets are charging to cash checks—$7 to $15 for a $500 Social Security check, an average charge of $12.87 for the first-time cost of cashing a $369 AFDC check. That's unbelievable.

You also say these outlets have sprung up in urban areas in the last 3 years.

Can you tell us, in your own opinion, what's going on and be very brief because the yellow light is on and I don't want to overextend my time?

Ms. **DUNLAP**. In my own opinion, what seems to be happening is that some of our poorer citizens are being taken advantage of and they don't have the options and the choices for a fairer system. So they are exposed to a certain amount of gouging.

Senator **METZENBAUM**. Thank you very much.

Thank you, Mr. Chairman.

Senator **DIXON**. I thank the distinguished Senator from Ohio.

The Senator from Missouri, Senator Bond.

Senator BOND. Thank you, Mr. Chairman.

There are a number of different areas that we want to pursue today, but I start off asking Mr. Brown, does your Connecticut law apply to savings and loans and credit unions?

Mr. BROWN. Yes, it does, Senator.

Senator BOND. What was the rationale? That all financial institutions should be required to cash checks?

Mr. BROWN. Yes, that essentially they are a depository institution and, with the exception of credit unions, they should all be required to cash the instruments without regard to whether or not there's an account there.

As to the credit unions, the payee must be a member of the credit union.

Senator BOND. Why?

Mr. BROWN. Because of the nature of the credit unions in establishing fields of membership. Traditionally, credit unions have provided services based on a membership basis, as opposed to being or allowing public access as do all the other depository institutions.

Senator BOND. Do I understand you that the State of Connecticut indemnifies the financial institutions for loss coming from improper payment on a check?

Mr. BROWN. No, sir. What we do is we rely—that was on a part of the question I answered previously—we rely mostly on the identification to ferret out fraudulent aspects. And the other is that——

Senator BOND. If a financial institution goofs up and pays the wrong payee, the State takes the burden, does it not?

Mr. BROWN. No, sir. The State forces the bank to rely on the uniform commercial code warranties that are inherent with any presenter of an item to be cashed. If the bank negligently cashes an item, then the bank absorbs the loss. If the bank does everything that is required by the regulations—i.e., looking at the three features of the two sources of identification—and it still is outwitted or a fraud is perpetrated on it, then that bank may apply to the Department of Income Maintenance for reimbursement.

Senator DIXON. Could I interrupt at that point, Senator? That intrigues me. Let's just take a case of a guy that got an Illinois driver's license fraudulently. He had a fake driver's license. It's got his picture on it and everything. And then had another fake document. I know it's a farfetched case. And the bank cashed it. It followed your rules and regulations, didn't it?

Mr. BROWN. Yes.

Senator DIXON. Then they would be protected, right?

Mr. BROWN. The bank would be protected.

Senator BOND. And the State bears the burden. So, in essence, the State is standing behind the banks. The financial institution doesn't have to pay that back. That's what I'm saying. The burden in your State is actually on the State of Connecticut and not on the financial institution if they follow the procedures you've outlined.

Mr. BROWN. With that condition, that's correct, Senator, provided they follow the dictates of the regulation and they do all of those things properly.

Senator BOND. But that's a major shifting of the burden. I think that's important to get on the record, if in fact the State does.

Mr. **Brown**. Well, that system was in place prior to the legislation. The only thing that we did by legislation was to require that all banks without regard to the person——

Senator **Bond**. I understand that, but I just——

Mr. **Brown**. That system was in place before the legislation.

Senator **Bond**. I think that's important to point out.

CHECK CASHERS ARE CONVENIENT

What do you think of Mr. Gagerman's contention that people use check cashers because they are more convenient than banks?

Mr. **Brown**. I think that banks have traditionally shunned certain working poor and also because of the structure of issuing these instruments on the 1st and the 15th of a month the banks actually dread those days when the welfare recipients will inundate their lobbies and I think out of a quest not to be treated disparagingly they go and they will pay extra money to not be looked upon disparagingly and unwanted. That's part of the problem. That's not a blanket indictment of all of them, but in my experience, if I could elaborate just a bit, I have traveled to the check-cashing services in Connecticut. I don't know of any that really adhere to strict percentage of instruments even though they advertise that they will charge 6 percent or 3 percent or 4½ percent, they were very arbitrary—those that I look at and cashed items before—as to what amounts they took for the payment of those services. That area needs regulation. It cries for regulation.

Senator **Bond**. Do you have any figures on how much the number of people cashing their checks increased at banks after the law was passed?

Mr. **Brown**. Do I have figures?

Senator **Bond**. Was there a major change?

Mr. **Brown**. No, there was no major change.

Senator **Bond**. Well, then that brings in the question on the validity of the law. If you still get the problems—I mean, are more people as a result of your law going in and cashing their checks at financial institutions?

Mr. **Brown**. No, Senator. The same number of people are going to more banks now, quite frankly, and it's less of a burden on the banks that decided to do the right thing initially. Bear in mind this law has only been in effect about a year and we're seeing some gradual transition. It's one thing to pass laws and it's another thing to get the word out and make it known and make these services available to inner city working poor.

Senator **Bond**. How are people advised that they can cash checks at banks? Do you put a notice in the check that goes out?

Mr. **Brown**. I have appeared before the media. I have done radio announcements to stations that broadcast mostly within the inner cities. We've also sought from the print media space free of charge to indicate that all banking outlets now will cash welfare checks.

The figures aren't available as far as whether or not there's been some mass movement from the inner cities to all of the branches available.

Senator **Bond**. But it seems to me that the simplest and most direct way to reach the recipients is to put a notice in with the check. Have you done that?

Mr. **Brown**. I believe we have done that. I'd like to check and verify it and make sure, but I believe we have done that.

Senator **Bond**. Because when you think about a targeted audience, that would be the simplest.

Mr. **Brown**. I believe we've done it. We have two departments here. I'm banking and that's only one of them.

Senator **Bond**. I wanted to follow up with Mr. Douglas on his comments that somebody who receives a Social Security check in the mail is 1500 times more likely to experience——

Mr. **Douglas**. I meant 1500 percent more likely. The ratio is 16 to 1; for every problem with a direct deposit payment there are 16—in fact it's a little more than that—problems with checks.

Senator **Bond**. The AARP statement to which my friend from Ohio referred says that only 47 percent of Social Security beneficiaries use direct deposits. So roughly half are direct and half are cash.

Mr. **Douglas**. It has gone up since then. It's right at the 50 percent mark, but that is essentially correct.

Senator **Bond**. So we've got a good balance. What's the basis of the 16 to 1 ratio?

Mr. **Douglas**. It's actual claims of nonreceipt by recipients where they have and report a problem.

Senator **Bond**. Well, I would like to ask Ms. Dunlap what her views on behalf of the Virginia organization are on the contentions of the AARP. Senator Metzenbaum asked that of Mr. Douglas. The AARP will testify that mandating direct deposit is undesirable because people are reluctant to use it. According to AARP, consumers have difficulty in resolving their problems and would miss their deposits and the financial institutions would have the potential for reaping large profits.

What are your views on that contention?

Ms. **Dunlap**. VCCC has the position in favor of consumers being able to choose the method. If they are more comfortable with direct deposits, if they've had good experience with that, they certainly should have the option. And if the banking industry wanted to release information to consumers to use either direct deposit or personal deposit, then I think that might be helpful if people knew more what the odds are.

However, we would still favor people being able to physically take the checks in and receive them personally if that's what they are more comfortable with.

Senator **Bond**. If I may pose just one more question, what about the testimony that Mr. Douglas gave that they're 16 times more likely to have problems with receipt by check than direct deposit? Do you feel that that is a reasonable claim based on your experience in Virginia?

Ms. **Dunlap**. I don't think that we have any statistics available independent of what the industry provides. I think information like that is helpful to consumers in making their choices. We would still like to preserve the right for people who prefer to use personal receipt of the check, if that's what they're comfortable with, to allow them to do that.

Senator BOND. Thank you, Mr. Chairman.

Senator DIXON. Thank you, Senator Bond.

May I say that we have another panel of five panelists, one additional panelist, and I know we've taken an hour and 20 minutes. We need to conclude by twelve with this hearing today. So I thought we'd better conclude in the next 10 minutes with this panel and I want to give my colleague from Ohio an opportunity if he has anything further to clarify between now and 10:30 before we go to the next panel.

But as chairman, may I ask—I think Senator Specter is here to introduce someone in the next panel, if my information is correct.

Here's some things the chair would like to have. From you, Mr. Brown, I would very much appreciate a copy of the Connecticut law and all the rules and regulations promulgated by the Connecticut government to support that law and any statistical experiences you have that would elucidate the Connecticut experience for the benefit of the members here.

And the final important thing that Senator Bond touched upon is there's a sort of inside debate here about how much this is really going to change things. For instance, if there's any way of clarifying this for me, I know from my own experience as a U.S. Senator from Illinois that in many of the inner city neighborhoods the place you cash your check is in a currency exchange. That's the facts of life. And I wonder how much that's going to change. That is to say, I got the impression from what you said to my friend from Missouri that it hasn't really changed that much in numbers of people doing it in Connecticut in the banks now as distinguished from check cashers before. Whatever you can tell us about how much change there is in actual experience out there by what we do would be helpful.

And, Mr. Douglas, from you, I wonder if there's any possibility that we could get, in cooperation between your department and the General Accounting Office, the kinds of experiences that you had that would help us in determining what is the cost of cashing Social Security checks and other things if all this is done and the loss experience and how much we need to build into the system for cost and for fraud and for losses and things of that kind.

Mr. DOUGLAS. Mr. Chairman, we would certainly be willing to try to do that, but some of the issues that you have raised I think really are beyond our knowledge. We know how much money we go after because of forged endorsements, but how much would it cost to a financial institution——

Senator DIXON. Maybe you and the General Accounting Office, working together, could give us a little something because you know more than we do.

And last, Mr. Gagerman, I didn't mean this to be picking on you, but I hear what you're saying to my friend from Ohio, you can't figure out how much it costs, but yet you can. I understand the risk in certain places of cashing these checks and all that kind of stuff, but there's got to be some way—I mean, there's a cost of doing business in whatever you do. Sometimes the cost is high and sometimes the cost is low. But in my State they make charges and there's some system they use to figure out what to charge, and it would be helpful to us to know that.

Let me say that if we're going to put another competitor out there against you, it doesn't mean we're putting you out of business. But we'd like to know something about the cost of doing business out there and I'd appreciate having whatever information you have. We'll be sending you written questions.

And then from you, Ms. Dunlap, your statistical experiences in your search in Virginia would be helpful to us and we'd like anything you could elaborate upon that.

Now there are 7 minutes left that I'd like to yield to my friend from Ohio because I think he'll get to the heart of other things that could be developed with this panel.

Senator METZENBAUM. Well, you're kind. I did have an opportunity to question so I don't want to impose upon the committee. I would just like actually to ask two questions.

Mr. Douglas, in the electronic payment, does the Social Security recipient and all other Federal recipients actually know the specific date on which the transfer is made?

Mr. DOUGLAS. In the case of Social Security, yes, sir, they do because it's the third day of the month. Various financial institutions have various ways, but almost all of them have numbers a person can call if the person is really concerned whether the payment was received, or the ATM's will also give that balance. So there are various ways of doing that.

But unlike third party checks, there is a fixed date, so people know that they're supposed to get the payment on this particular date. SSI payments have to be there on the first and railroad retirement is also the first.

Senator METZENBAUM. Are those specific dates for the railroad retirement checks?

Mr. DOUGLAS. Yes, sir. Also, veterans benefits and civil service retirement payments are received on the first of the month. Direct Deposit is a much safer, more reliable and less expensive approach to making payments and the recipient gets the availability and use of those funds earlier, Senator.

If this test in Baltimore we were talking about earlier is successful, it opens up the avenue to your other bill, S. 907, which is lifeline banking, because at least—I'm not a banker, but it seems to me it's certainly possible that through direct deposit, electronic deposit into the account, which is a lot less expensive for banks to handle than mailed in or walked in checks, and through withdrawals through either point of sale terminals or ATM's, that you really I think overcome a lot of the problems that banks have indicated they have with a lifeline banking account.

So I think it has a lot of potential and I really am looking forward to seeing the results of that test.

Senator METZENBAUM. I thank you.

FEW CHANGED OVER

Mr. Brown, I think all of us opened our eyes when you said that although Connecticut has a good law, very few are using it.

Can you give us some factual basis for that because it's sort of an astounding reality that people can get their checks cashed for free and they're still paying for it. What can you tell us about that?

Mr. Brown. Thank you, Senator, for an opportunity to get back to that point.

One thing that must be recognized is that the law became effective in October 1988. Second, it only applies to welfare checks. There are other instruments that poor people use which would not be acceptable before a bank or a branch office because they don't have accounts there. To establish accounts at those branches would require a disproportionate amount of cost. It requires fees. For those that don't have lifeline banking it requires an inordinate amount of cost given the level of income of these people.

Senator Metzenbaum. But it doesn't require any cost if you have a welfare check to walk in the bank and cash it, does it?

Mr. Brown. That's correct. And I don't want to give the impression that that's not being used. It's merely that I do not have quantifiable data given from October 1988 when this thing first passed to really give you hard figures.

Senator Metzenbaum. I think we all would like to know that and I'm sure the chairman would accept some supplemental information from you on that subject.

Thank you, Mr. Chairman.

Senator Dixon. I thank you very much, Senator Metzenbaum.

The distinguished senior Senator from Connecticut, I had indicated earlier, wanted to be here, Commissioner Brown, while you were here out of his high regard for you. He had a speaking engagement this morning that prevented him from getting here until now and I know at great difficulty has arrived here. We're honored to have the distinguished Senator from Connecticut here.

Senator Dodd. Thank you very much. My colleague from Illinois has taken over the chairmanship of this subcommittee and I had the pleasure of having it for a couple of years. I wasn't sure how he would handle this job, but since he's having you back as a witness, we know the tradition carries on.

I won't take up the time, Mr. Chairman. I know you've already covered a lot of the ground on the issues before us. Senator Metzenbaum, of course, had a deep interest in the legislation we had a year or so ago. In Connecticut we've had, as Howard no doubt has expressed, a Connecticut law affecting State public assistance checks. Of course the Metzenbaum bill would require depository institutions to cash government checks up to $1500.

What I'll do, Mr. Chairman, is submit some questions rather than belabor it now.

Senator Dixon. May I say to my friend from Connecticut, Commissioner Brown has been very, very helpful in telling us about the Connecticut experience. He's going to make the law and all the regulations promulgated in support of that law available to this subcommittee. I want you to know that I will confer with you personally about that, Senator, and we are honored to have you in the subcommittee today and appreciate your coming.

Senator Dodd. Thank you, Mr. Chairman, and I thank all the witnesses for coming.

Senator **Dixon**. We thank you all very much. I will be sending written questions to every one of you. What you are telling us is very helpful in arriving at a decision that I think will be arrived at sometime in the next month or so and we thank you for giving your valuable time and we'll call the second panel now and we thank you very much, ladies and gentlemen.

The second panel is Robert L. Stevens, president of Bryn Mawr Trust Co. in Bryn Mawr, PA, representing the American Bankers Association; Richard A. Loundy, of my State, chairman of the board of Devon Bank, representing the Independent Bankers Association of America; John P. Kelly, Jr., president of the National Bankers Association in Washington; Peggy Miller, legislative representative of the Consumer Federation of America; and Robert J. Sell, member of the National Legislative Council, American Association of Retired Persons in Chicago.

Mr. Stevens, you're fortunate in having a distinguished Senator from your State who has made a visit here to introduce you and I recognize the distinguished Senator from Pennsylvania, Senator Specter, for that purpose.

OPENING STATEMENT OF SENATOR SPECTER

Senator **Specter**. Thank you very much, Mr. Chairman.

Since it is a large panel and all the seats are filled, if I may, I will stay here for the purpose of making an introduction of a very distinguished Pennsylvanian who will be testifying here today, Mr. Robert L. Stevens.

Bob Stevens is the president of the Bryn Mawr Trust Co. He was born in Waukegan, IL, which may provide some special credential for this subcommittee.

Senator **Dixon**. In his youth he was a man of sound judgment.

Senator **Specter**. Or his mother was—his parents were being located there. But he exhibited that sound judgment beyond when he was educated at Northwestern University and then he demonstrated even sounder judgment in becoming a Pennsylvanian, Mr. Chairman, because he has been a Pennsylvanian and he became the president of Bryn Mawr Trust in 1980, which was a vintage year when you and I, Mr. Chairman, were elected to the U.S. Senate.

Of special interest I think is the fact that he's succeeded in the presidency by Mr. Clyde Hart of Bryn Mawr Trust whose brother was Phillip Hart, a very distinguished U.S. Senator for whom the Hart Senate Office Building is named. Senator Hart, having been a native Pennsylvanian as well, I don't wish to bring up the issues of judgment, but we all know Senator Hart ended up in Michigan. That goes to show that we are a moving society.

On the subject of Mr. Stevens, he has a very distinguished academic career. After his work at Northwestern, he has done graduate work at the Columbia School of Business, Drexel University, and at the Stonier Graduate School of Banking. He has been very active in the banking profession. He serves on the board of directors of the American Bankers Association. He serves as second vice president of a Pennsylvania Banking Association and beyond his technical and professional skills, he's known as a man of understanding and of compassion and very deeply involved in matters of public and communal affairs.

So when I heard he was going to be here to testify this morning I wanted to stop by to make this presentation and to vouch for his testimony.

I wish I could stay but at this moment we're having a Judiciary Committee hearing where we're going to be considering the nomination of the Deputy Director for Drug Enforcement. So I'm going to have to absent myself, but I do appreciate this opportunity, Mr. Chairman.

Senator DIXON. I thank you, Senator Specter, and I know Mr. Stevens appreciates the fact that you would take time out of your busy schedule to come here and honor him by introducing him.

Ladies and gentlemen, the situation is that we will put your full statement in the record. You each have 7 minutes to make your statement. I would appreciate it if you would confine your remarks to that time. When the red lights comes on I move on.

Mr. Stevens, we're delighted to have you here.

STATEMENT OF ROBERT L. STEVENS, PRESIDENT, BRYN MAWR TRUST CO., ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. STEVENS. Thank you, Mr. Chairman.

I'm pleased to testify today on behalf of the American Bankers Association.

This hearing is part of a search for the best means for encouraging cooperative efforts between the government, banks and community groups in addressing our shared concerns.

Now the ABA is the national trade association. We represent commercial banks of all sizes, types and locations with our members' combined assets representing approximately 95 percent of the industry's total.

Whatever the endeavor, there is room for improvement, but bankers do not believe they are getting adequate credit for the great deal they have already achieved. More than half of all banks and nearly three-quarters of large banks already offer low-cost basic banking accounts. You will hear different numbers from some whose criteria are so rigid that my own bank's low-cost account is excluded from their totals. I suggest that we beware of the numbers.

Nearly 90 percent of all banks already are willing to cash government checks for noncustomers and free checking is available to senior citizens at nearly 80 percent of banks. Banks throughout the Nation are active participants with community groups in projects designed to better their towns and their neighborhoods.

Let's judge banks based on real data, not on horror stories told to this committee in the past which turn out baseless upon investigation.

Mr. Chairman, the questions which you asked me to address in my oral testimony are a good way to begin finding answers.

First, you asked why there is a check cashing problem. There is a problem primarily because some low-income individuals do not have bank accounts. If they had an account with a bank or other depository, they could get government checks cashed. Many are simply unaware that needed services are available from local banks at low cost. The ABA will encourage banks to communicate that availability.

Another problem is that some people are simply uncomfortable dealing with banks, often because of illiteracy or lack of English fluency. Still others are concerned that they may overdraw their account even though overdraft protection may be available. In sum, habit, lack of information, and educational and sociological barriers play a far larger role than the availability or pricing of such bank services.

Your second question regards potential benefits of encouraging or requiring direct deposit of government benefit checks. Direct deposit is faster, less prone to fraud and theft, and less expensive for depositories and for the government.

The success of the Social Security Administration's voluntary direct deposit program and surveys of similar programs demonstrate that recipients perceive real benefits and prefer the utilization of new technologies over the old system of getting a paper check in the mail. The virtues of direct deposit are so overwhelming that it's clearly the wave of the future in public assistance delivery systems.

The second part of that question asked whether we would support more effective regulation of nonbank currency exchanges. We are not sufficiently acquainted with any present regulation of their fees and policies or complaints directed against them to give a fully informed answer.

However, since government benefit recipients turn to exchanges as well as to grocery stores and to other businesses to cash their checks, the task of fully regulating all providers would appear to be daunting.

Now your third question asked for the best ways to minimize fraud in the cashing of government benefit checks. One of the best is direct deposit. However, if an identification card system is going to be utilized in conjunction with mandatory cashing of paper checks, we believe that government should be the issuer of the cards and should also be willing to indemnify depository institutions against fraud losses.

Further, depository institutions must have discretion to exercise expertise and judgment to refuse a check where they suspect a fraud and each institution should be able to charge a fee based on its own cost.

Your final question asked whether everyone should have a checking account. Eight out of nine American families already have a depository account relationship. One hundred percent probably never will due to a variety of personal and sociological factors.

We believe that through cooperative efforts and without legislative mandates we can achieve a situation in which everyone that wants a bank account has one.

Mr. Chairman, my written testimony documents the exciting new programs utilizing modern technology to deliver government benefits to citizens. This subcommittee can be a focus point for disseminating information about such programs. Modest Federal seed money for additional pilot projects might speed solutions. Any of those routes is preferable to mandating that recipients of government benefits be locked into yesterday's approaches and that banks be locked into a system that's too expensive and permits fraud and abuse.

And solutions must reflect local conditions. If banks are asked to be sensitive to local needs, then how can it make sense for Washington to mandate one rigid approach which is supposed to meet the needs of all our diverse communities?

My written testimony discusses the recent Federal banking regulator harmonization of CRA supervision and enforcement. It also relates major CRA commitments banks are voluntarily entering. We believe that CRA is working well already, but that improvements should be made through cooperation, not confrontation.

And as this committee is well aware, CRA can only supplement but cannot substitute for public sector commitment to housing and to urban development.

Mr. Chairman, bankers do understand civic responsibilities. They understand fully that their banks' fortunes are linked to its home communities. Bankers will try harder, but they would like due credit for all they have already achieved.

We are ready and willing to work with Congress, but we don't want to be required to provide rigid solutions to problems which we're addressing through flexible approaches or to open ourselves up to fraud or to ask some of our customers to deeply subsidize service to others.

Other questions must be addressed. What level of low-income services and community commitment will be judged enough? Why are our ever more successful nonbank competitors exempt from such requirements and expectations, even though they offer the same product types and draw deposits and investments from communities throughout America? Why should credit unions with a communitywide common bond be exempt from CRA requirements? Why are not insurers asked to provide basic life and health and auto insurance?

Mr. Chairman, today's hearings are an excellent opportunity for beginning to answer your questions and ours. We look forward to working with you in addressing our shared concerns.

I thank you.

[The complete prepared statement of Robert L. Stevens follows:]

STATEMENT OF

ROBERT L. STEVENS

PRESIDENT, BRYN MAWR TRUST COMPANY

ON BEHALF OF

THE AMERICAN BANKERS ASSOCIATION

BEFORE

THE SENATE SUBCOMMITTEE ON

CONSUMER AND REGULATORY AFFAIRS

CONCERNING

OVERSIGHT ON GOVERNMENT CHECK CASHING,

BASIC BANKING, AND THE COMMUNITY REINVESTMENT ACT

JUNE 6, 1989

Summary of Testimony of Robert C. Stevens on behalf of the ABA regarding Consumer Issues and Community Reinvestment

June 6, 1989

Introduction (pp.1-4)

- Banks are not receiving due credit for their present low-income services and community reinvestment activities.
- Check cashing problems stem more from sociological factors and communication deficiencies than from lack of availability or high cost.
- Direct deposit of benefits is demonstrably superior to paper check distribution and is preferred by beneficiaries.
- More extensive regulation of nonbank currency exchanges would be difficult to enforce.
- Any mandatory check cashing proposal must include government issuance of identification cards and indemnification to banks for losses. Basic banking mandates should also include indemnification.
- Eight out of nine American families already have a deposit account. Our joint challenge is reaching the remaining group as best as possible.
- Government can play a useful role by compiling information and encouraging innovation and public and private partnerships.

Basic Banking and Government Check Cashing (pp.5-18)

- Half of all banks, and three-quarters of large banks, already offer basic bank accounts. Nearly nine out of ten banks already cash government checks for noncustomers.
- Anecdotal evidence of service deficiencies presented to the Committee in 1988 were incorrect.
- S.906 still lacks adequate safeguards against fraud losses due to mandatory nondiscretionary check cashing.
- Direct deposit is a superior alternative already chosen voluntarily by a majority of Social Security recipients. The U.S. Government has many successful electronic benefit services (EBS) underway, as do states and localities.
- Banks should not be required to offer subsidized services, especially when nonbank competitors are exempt.
- A Federal Reserve mandated uniform fee for check cashing or basic banking services will fail to cover many banks' costs.
- Mandatory, rigid, and nondiscretionary check cashing and/or basic banking requirements could be counterproductive, leading to some closings of marginal branches in low-income neighborhoods.

- o Nearly eighty percent of banks offer free checking accounts to older Americans.
- o S.907 does not adequately protect banks against fraud or mismanagement in the use of basic bank accounts.

Community Reinvestment Act (pp.18-27)

- o CRA is working well, fostering bank and community dialogue and cooperation.
- o CRA focus should not be shifted from applications to the examination. It would replace a cooperative process with a confrontational event and create pressure on the examiner to be a dispute mediator rather than an impartial fact-finder.
- o CRA successes can be encouraged best through information-gathering and communications efforts.
- o Disclosure of CRA ratings and reports would have detrimental effects. The banking regulators' joint policy statement is a more promising approach which should be given an opportunity to prove itself.
- o CRA cannot solve all community problems; it cannot substitute for requisite public sector responses.
- o Nonbank financial providers should be required to comply with CRA-type standards before commercial banks are asked to assume a greater burden which our competitors are exempt from. Banking's share of credit and financial services has been steadily declining.
- o Ongoing projects in Atlanta, Philadelphia, Chicago, the Twin Cities, Boston, and St. Louis are some illustrations of the diversity of banking's CRA commitment. ABA is actively encouraging expanded efforts.

Conclusion (pp.27-29)

- o America's bankers are ready and willing to work with Congress and consumer and community groups.
- o Programs must be fair and equitable among all financial providers.
- o Regulatory burdens must be minimized.
- o Federal efforts must not inhibit ongoing innovations across the U.S.
- o Solutions must be flexible enough to be applicable to the diversity of American communities.

Appendix (pp.30-32)

Cites additional state and local efforts and statutory requirements.

STATEMENT OF
ROBERT L. STEVENS
PRESIDENT, BRYN MAWR TRUST COMPANY
ON BEHALF OF
THE AMERICAN BANKERS ASSOCIATION
BEFORE
THE SENATE SUBCOMMITTEE ON
CONSUMER AND REGULATORY AFFAIRS
CONCERNING
OVERSIGHT ON GOVERNMENT CHECK CASHING,
BASIC BANKING, AND THE COMMUNITY REINVESTMENT ACT

JUNE 6, 1989

Mr. Chairman and members of the Subcommittee, my name is Robert L. Stevens and I am President of the Bryn Mawr Trust Company in Bryn Mawr, Pennsylvania. I am pleased to appear before you this morning to testify on behalf of the American Bankers Association (ABA) regarding the obligations of commercial banks to the communities which they serve and to the less advantaged members of those communities, as well as the best means for encouraging cooperative new efforts between all levels of the government, the banking industry, and community groups in addressing our shared concerns. The ABA is the national trade association representing commercial banks of all sizes, types, and locations. The combined assets of our members represent approximately 95 percent of the industry total.

Mr. Chairman, although my own bank is not located in a low-income area, it has nonetheless supported a number of projects benefiting the surrounding community. Further, as Chairman of ABA's Community Involvement/Consumer Compliance Task Force, I have been actively involved in banking industry efforts to identify the most pressing consumer and community reinvestment issues and to make recommendations to the ABA's Board of Directors, on which I serve, as to how the ABA can better help all of its members to establish working relationships with community groups and to develop programs which satisfy consumer and community needs.

In every field of endeavor there is room for improvement, and I would not tell you that there is no room for improvement in the banking industry's response to the needs of low-income individuals and some of our troubled communities. But, at the same time, I would not be frank if I did not say that bankers do not believe that our industry is getting adequate credit for the great deal that they have already achieved. More than half of all banks and nearly three quarters of large banks already offer low cost basic banking accounts throughout America. More than 80 percent of all banks already are willing to cash government benefit checks for noncustomers. And banks throughout the nation, some of which are cited in my full testimony, are active and full participants with local community groups in projects designed to better their towns and neighborhoods. Listening to some of our critics, you might think that the banking industry was getting F's on its report card and that only government discipline could raise the level of achievement to a C. I think the reality is that the industry as a whole is doing a solid job right now. That is not to say there are not specific problems, and we are here today to discuss the most promising routes to getting that performance up to an A.

Mr. Chairman, the questions which you have asked me to address in my oral testimony are a good way to begin finding those answers.

First, you asked why there is a check cashing problem. There is a check cashing problem because a group of individuals, primarily those with very low incomes, do not have bank accounts. If these individuals had an account with a bank or other depository institution they would have no problem getting their government check cashed. Since a majority of banks, especially those in urban areas, offer basic bank accounts at low cost, and since banks are generally willing to cash checks for noncustomers at lower cost than other check cashing services, cost is not the primary reason for the problem. We certainly recognize that any expense is a problem for low-income individuals, but many of these basic banking accounts are offered more or less at their cost to the institution; in other words, in most cases banks would have to subsidize the account, as some already do, in order to lower the cost.

One of the greatest barriers appears to be that these individuals are simply not aware that services they need are available from local depository institutions at low cost. The ABA is going to do everything we can to encourage banks to communicate this availability. Another reason is that some individuals are simply uncomfortable dealing with banks, a feeling often compounded by illiteracy or a lack of fluency in English. Still other individuals are concerned that they may overdraw their checking account, resulting in a penalty fee, but they may not be informed as to the availability of overdraft protection. In sum, habit, lack of information, and educational and sociological barriers play a far larger role than the availability of such services from banks or their cost.

Your second question regards the potential benefits of encouraging or requiring direct deposit of government benefits. Direct deposit is certainly faster, less prone to fraud and theft, less expensive for depository institutions and units of government, and can be designed to result automatically in the establishment of an account which can be the basis of greater financial self-management. As my testimony recounts, many states and localities have already adopted either direct deposit of their benefits and/or electronic access to them as a means of maximizing these positive results. The growing success of the Social Security Administration's voluntary direct deposit program, as well as surveys of participants in similar programs, demonstrate that recipients perceive these real benefits and prefer the utilization of such new technologies over the old system of receiving a paper check in the mail. We think the virtues of direct deposit of government benefits, often in combination with electronic access to them, are so overwhelming that this is clearly the wave of the future in terms of public assistance delivery systems.

The second part of that question asks whether we would support more effective regulation of nonbank currency exchanges. We are not sufficiently acquainted with their present level of regulation, if any, their fees and policies, and any complaints directed against them to provide a fully informed answer in this regard. However, since recipients of government benefits who do not utilize depository institutions turn to such check cashing exchanges as well as local groceries and other community business, the task of fully regulating all of these providers would appear to be somewhat daunting. Again, the best answer would seem to be a program of education and full information for low-income individuals so that they fully understand their alternatives and will know if they are being charged an unfair price. In addition, general consumer fraud statutes should certainly be applied.

Your third question asks what are the best ways to minimize fraud with regard to the cashing of government benefit checks. One of the best ways, as I just discussed, is to deposit directly those benefits in the recipient's designated depository institution. However, if some type of identification card system is going to be utilized in conjunction with the cashing of paper checks, we believe that it is the government which should have the responsibility of issuing the identification card and that the government must be willing to indemnify depository institutions against any fraud losses which they incur under a mandatory program. Further, depository institutions must be granted fairly broad discretion to exercise their expertise and judgment to refuse to cash a check where they believe that a fraud is being perpetrated.

Your final question asks whether everyone should have a checking account. As my testimony notes, eight out of nine American families already have an account relationship with a depository institution. ABA supports the basic banking account concept, and we believe every American should be able to have an affordable checking or savings account if they wish to do so. Eighty-eight percent already do. One hundred percent probably never will due to a combination of personal and sociological factors; so what we're really discussing today is how to get from 88 percent to somewhere in the mid-90's. Government needs to do a better job of conveying to low-income individuals the benefits of establishing an account relationship, and the banking industry needs to do a better job of communicating the wide availability of affordable basic banking accounts. We believe that through cooperative efforts and without legislative mandates we can achieve a situation in which everyone who wants a bank account has a bank account.

Mr. Chairman, much of my extensive written testimony documents the many exciting new programs which utilize modern technology to deliver government benefits to our citizens without unnecessary costs or fraud. This Subcommittee can serve as a focus point for gathering information about such programs and disseminating that data to spur replication throughout the United States. You can work with your colleagues throughout the Congress in encouraging the utilization of such technologies to the maximum extent possible. You can consider whether some modest amount of Federal seed money for pilot projects could not have a tremendous affect on the development of such solutions. Any of those routes would be preferable to mandating that the recipients of government benefits be locked into yesterday's approaches and that banks be compelled to participate in a system that is unnecessarily expensive and open to fraud and abuse.

My testimony also documents the innovations which have been made in the design and offering of basic bank accounts. These accounts are available today, and the real challenge is communicating that availability to potential users. If banks are being asked to be sensitive to local community needs, then how can it make sense for Washington to mandate one specific nationwide account which somehow is supposed to meet the needs of all the diverse communities throughout the United States?

Finally, my written testimony discusses the recent move by the federal banking regulators to harmonize their Community Reinvestment Act ("CRA") supervision and enforcement, as well as a number of the major commitments banks are voluntarily entering into in cooperation with community groups. One goal of the ABA Task Force which I chair is to encourage similar efforts throughout the nation.

Mr. Chairman, the great majority of bankers do feel a civic responsibility to all members of their community and have an instinctive understanding that their bank's welfare is directly linked to the communities in which it operates. Bankers are willing to try harder, but they also would like to get some credit for all they have already achieved. We are ready and willing to work with Congress but we don't want to be required to provide rigid "solutions" to problems which are being addressed; or which could be better addressed through flexible approaches; or to open ourselves up to fraud; or to ask some of our customers to deeply subsidize services to others.

There are other questions which need to be addressed. What level of service to the disadvantaged and commitment to our communities will be judged to be doing "enough" and who is capable of making that judgment? Why are our ever more successful nonbank competitors exempt from such requirements and expectations, even though they are offering the same types of products we are and are drawing deposits and investments out of local communities throughout America? As increased costs are imposed on the banking industry, our competitive disadvantage will only grow, resulting in more and more money flowing to institutions with little or no community involvement. Why, for example, should credit unions with a community-wide common bond be exempt from CRA-type requirements?

Other questions relate to how we can encourage more state and local government/bank cooperative efforts; how we can better educate low-income consumers as to the advantages of direct deposit; and what governments themselves can do to lessen the potential for fraud and lower the costs for cashing checks.

One final range of questions relates to the ability of adopting one solution for all types of banks in all types of communities. How can a solution designed for urban areas, served mostly by large banks, for example, be relevant to a rural community served by a very small bank? And yet many proposed "solutions" would do just that -- treat the problem as though it were the same everywhere.

Mr. Chairman, today's oversight hearings present an excellent opportunity for beginning to answer both your questions and ours. We look forward to working with you and the other members of the Subcommittee in addressing all of our shared concerns.

BASIC BANKING AND GOVERNMENT CHECK CASHING: BACKGROUND AND SUMMARY

One focus of this hearing is proposals to require depository institutions to offer basic banking accounts to the general public and to cash government checks for noncustomers. A primary concern prompting such ideas is that because a certain percentage of the population does not maintain bank accounts some recipients of government benefit checks may have difficulty cashing those checks, or may have to utilize expensive alternatives such as check cashing facilities.

Mr. Chairman, America's bankers are very sympathetic to this concern. We are anxious to work with Congress, the Administration, and state governments to ease any problems in cashing government checks and to increase the number of persons with bank accounts. ABA endorses the concept of basic banking and believes that banks should endeavor to design products which respond to the particular demands and needs of their full potential customer base. In this spirit, in 1985 we took the lead in urging our banks to provide low cost checking services in their communities. Every member bank received an ABA "Voluntary Effort" kit which addressed three consumer issues and included advice on designing a basic bank account. Bankers have responded positively. Our 1986 survey showed 47 percent of banks offered basic bank accounts. Today, our latest survey reflecting 1988 data showed an increase to 53 percent, with an additional 8 percent planning to offer them. At large banks, those most likely to serve urban areas, more than 73 percent now offer such accounts. Similarly, a 1985 Government Accounting Office ("GAO") report found that 86 percent of banks cash checks for noncustomers, and our own recent survey confirms that finding.

My own bank has for over 28 years offered a basic bank account. This account requires no minimum balance, costs only $2.00 per month, and allows seven checks per month for free. Additional checks cost $0.25 each. In addition, Bryn Mawr Trust cashes state, local, and U.S. Treasury checks for noncustomers without charge, as long as they produce appropriate identification.

In spite of the widespread availability of basic bank services, anecdotal complaints are often used to generate general conclusions to the contrary. To illustrate, last year in hearings before the Senate Banking Committee, Mr John Gleeson, from the New Jersey Department of the Public Advocate, specifically cited three cases where banks declined to cash checks for noncustomers, and benefit recipients were compelled to pay check cashers high fees. Yet, a quick survey of some of the banks in those areas show that basic bank accounts are available at no and low charge in each of the areas identified.

A Camden County, New Jersey woman complained that a bank refused to cash her Social Security check which was drawn "on a bank in Birmingham, Alabama." A limited survey of banks in that county revealed that two banks offer free accounts to the general public with no minimum balance requirement and two others offer such free accounts to senior citizens. Five banks offer accounts for $2.00 and under and require no minimum balance.

Mr. Gleeson related that a Middlesex County woman paid $36.00 to cash a $436.00 check at a check cashing facility after several local banks refused to cash it because she had no account with the bank. Yet, for far less than $36.00 per month, she could open an account with as little as a $10 initial deposit. Our survey identified four banks which offer free accounts for $2.00 or less per month and require no minimum balance; some charge a small per check charge. One bank offers a free account so long as $50.00 is maintained in the account.

The final complaint was from a woman in Mercer County. Because a bank refused to cash her benefit check, she had to travel 18 miles to cash it at a check cashing store. Our survey found one Mercer County bank which offers free accounts with no minimum balance requirement to the general public, another bank which offers free accounts to seniors, no minimum balance required, and a third bank which offers accounts for $2.00 per month, no minimum balance required. A fourth bank offers an account for $2.00 per month so long as $50.00 is maintained in the account.

Thus, while these individuals brought specific complaints about being forced to use expensive check cashing facilities, cheaper service are available to them in the form of basic bank accounts.

ABA has also been active in promoting the development of electronic delivery of government benefits as a means to improve their delivery to those without bank accounts. And, in 1977, we began a national volunteer Personal Economics Program (PEP), in which bankers work with teachers in familiarizing students with banks, banking services, and personal financial management skills. The program is administered by state banking associations and other bank organizations. PEP has reached more than one half million students each year for the past five consecutive school years.

Some proponents of mandatory legislation seeking to increase access to bank accounts tend to overlook some of the broader social reasons why some individuals shun banks in favor of check cashing facilities. Many of these reasons are not related to the cost of a basic bank account or to any reluctance of banks to cash government checks for noncustomers. Indeed, the Consumer Federation of America concluded in its September 1987 "National Survey of Check Cashing Outlets" that consumers would generally pay less at banking institutions than at check cashing centers and would get more for their money. Other studies agree that those without bank accounts seldom cite high service charges or minimum balance requirements as the reasons they lack an account.1/

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1. "Basic Banking," Federal Reserve Bulletin, April 1987, pp. 262-265.
"Low-Income Banking Needs and Services," Journal of Retail Banking, Fall 1988, pp. 33-37.
"Survey of Low-Income Households Without Checking Accounts," Unidex Corporation; March, 1985.

Some of the reasons given by these individuals for using nonbank alternatives include:

- comfort with their present personal cash management system;
- perceived simplicity of the check cashing and money order system compared to bank account;
- desire for close personal control over money and/or lack of familiarity with banks;
- inconvenience of bank location or business hours;
- illiteracy and innumeracy;
- perceived inability to manage a checking account and know its current balance;
- fear of overdrafts;
- lack of minimal fluency in English;
- belief that they have insufficient funds and/or transactions to justify having an account.

Many programs are currently in place or under development aimed at improving access to government benefits, particularly for those without banking accounts. Using electronic alternatives, these programs deliver food stamps, welfare benefits, Supplemental Social Security income ("SSI"), and Aid to Families with Dependent Children (AFDC). Such programs, while still emerging, show great promise as superior remedies in terms of safety, convenience, efficiency, and minimum fraud. The October 1988 GAO Report to Congress, "Government Check Cashing Issues," reported that "use of electronic funds transfer technology, for example, has been cited as a way to solve check cashing problems by bringing more government check recipients into the banking system."

ABA is concerned that a single, Washington-mandated "solution" for basic banking and government check cashing services will stifle innovation in such electronic programs as well as imaginative basic bank accounts responding to local needs and conditions. Further, we are concerned about the fraud potential, costs, and compliance burdens which inevitably would accompany rigidly mandated responses which rely on yesterday's practices and technologies. Electronic alternatives to the paper check, while still emerging, show great promise as superior remedies in terms of safety, convenience, efficiency, and minimum fraud. ABA's enthusiasm for direct deposit is demonstrated by our in-house promotional program, as a result of which eighty-five percent of our employees have voluntarily chosen to receive their salaries in this manner.

MANDATED GOVERNMENT CHECK CASHING

Some proposed legislative solutions, such as S.906, continue to contain major flaws. While S.906 represents an improvement over earlier proposals, it still imposes risks on the banking industry by requiring that we assume the good faith and proper identity of individuals presenting checks apparently drawn on government entities. Though S.906 contains measures intended to protect depository institutions against losses due to potential fraud, they are inadequate. A high degree of risk persists under the bill irrespective of those provisions.

S.906 would require depository institutions to cash government checks up to $1,500 if the person presenting the check is the payee and is registered with the depository institution. The depository institution could charge a fee for the service so long as the fee does not exceed the limit established by the Federal Reserve Board ("Board"). Depository institutions would have to permit the customer to designate at least three separate branch offices where the customer may cash the check upon presentation of a copy of registration and an identification card. The depository institution would have to cash the check even if it reasonably believed the check to be forged, altered, or counterfeit. Services would not have to be extended to individuals who hold a transaction account or a government check cashing relationship at any other depository institution, although it is not clear how another bank could know such facts.

The Board would prescribe regulations to establish registration requirements. Such regulations would allow the depository institution to require an applicant to present an identification card which includes the signature and photograph of the customer. A depository institution could reject a registration if it determined that an "intentional material misrepresentation has been made."

For purposes of the bill, "government check" is defined as any check issued by the United States or agency thereof; any state, regardless of the location of the depository institution; any agency of the state in which the check is presented; and any unit of local government of that state or agency thereof.

The Board could promulgate regulations to ensure that any individual would have the right to have any recurring government check directly deposited.

Direct Deposit, Electronic Access, And Other Emerging Programs Offer Reasonable Alternatives To Mandated Government Check Cashing

Legislation such as S.906 may do a disservice to government benefit recipients by perpetuating a method of payment which does not best serve them. Mandated government check cashing perpetuates the paper check distribution of payments and thereby discourages the exploration and development of less expensive and more efficient, secure, and convenient alternatives. For example, direct deposit payments into a beneficiary's account have these advantages:

- Recipients have immediate access to those funds. They do not have to wait for the check to arrive in the mail and then deposit it personally.
- Recipients are protected from theft of the check itself and theft of the cashed funds; this benefit is of particular value to elderly and handicapped Americans. Recipients are not compelled to carry large sums of cash, but may draw funds as needed.
- Direct deposit encourages recipients to establish and maintain accounts and may thereby encourage savings and financial planning.

- Direct Deposit is less expensive for all levels of government as well as for banks with the capacity to accept direct deposits. The Treasury estimates that the cost of delivering a paper check is 26 cents more than the cost of a direct deposit payment.

It is also worth noting that although the Treasury only began making direct deposit available in 1975, by 1988 48 percent of Social Security payments were made by direct deposit. The Social Security Administration estimates that, by 1990, at least 60 percent of recipients will receive benefits electronically. The high percentage of Social Security recipients adopting direct deposit in a relatively short period presents persuasive evidence that social security recipients find direct deposit to be highly acceptable because it offers real advantages. Contrary to some misinformed claims, millions of Social Security recipients do not disdain direct deposit as undignified but are glad to have the safety and convenience offered by this modern delivery mechanism.

Promising Developments

Other convenient and practical alternatives to paper checks are in the process of development. These programs rely on electronic payments, ATMs, and special access cards. Thus far, they show great promise. In fact, the GAO's 1988 report "Government Check-Cashing Issues," concluded, "If Congress determines that recipients of certain government checks should not bear these costs [the costs associated with the cashing of government checks] or should be assured of a low cost option, it should consider encouraging methods that utilize plastic cards and electronic funds transfer technology."

Thus far, evaluations of these electronic benefit service (EBS) programs show a high level of satisfaction among benefit recipients. The projected potential benefits are being realized. The target groups of many of these programs are those individuals who lack bank accounts.

In 1984, the Food and Nutrition Services (FNS) of the United States Department of Agriculture began operation of such an EBS program as part of a general effort to improve the efficiency and integrity of food stamp issuance and redemption. Under this program, check-out counters in participating stores were equipped with teller machines. Beneficiaries presented a magnetic striped card and entered their personal identification number. A deduction was then made from the customer's "authorization account." An evaluation of the program concluded that recipients strongly prefer the electronic benefits system (77 percent to 17 percent) because of its convenience and ease of use. The evaluation found strong preference for the EBS system among the handicapped, non-English-speakers, and recipients with little education.

Following that successful pilot, in order to learn more about the potential for EBS technologies, FNS is currently gearing up similar programs with varying features. Four pilots -- in Arizona, Minnesota, New Mexico, and Washington -- are under development and expected to begin operation in February 1990.

The Social Security Administration, in conjunction with the Financial Management Services of the Department of Treasury, is also preparing a pilot to distribute SSI to recipients who are blind, disabled, or aged. Its purpose is to improve service to beneficiaries who generally do not maintain bank accounts. The pilot is expected to begin October 1989 in Baltimore, Maryland.

State and local programs are also in operation or development. The Maryland State government is in the process of designing a program to deliver both federal and state benefits through a single magnetic-striped card. Food stamps, AFDC payments, and state welfare benefits will be accessed through ATMs (using the regional MOST network) and point-of-sale terminals located in retail stores. The state government hopes to reduce dramatically the paperwork burden associated with the current system and to expedite distribution of benefits. That program is scheduled to begin operation this August.

The results of a pilot program in Minnesota which distributes welfare assistance benefits electronically have been so positive that the pilot has been extended and will probably become permanent. Briefly, the Minnesota program allows recipients to access benefits from ATMs and operator-assisted teller machines using magnetic striped identification cards, personal identification numbers, and other means of identification. Of the approximately 700 participants surveyed, an overwhelming 88 percent of participants preferred electronic delivery, only 4 percent preferred checks, and the remaining 8 percent expressed no preference.

In New York City, public assistance and food stamp recipients now receive benefits through use of magnetic striped cards, eliminating approximately 200,000 annual incidents of lost or stolen benefits. This new system has reduced municipal public administrative expenses by $11 million.

In addition to such local programs, the Financial Management Services of the Department of Treasury has been assiduously studying the matter of distribution of government payments during the last year. They have organized work groups comprised of representatives from the banking industry, supermarkets, check cashing facilities, consumer groups, participants in current EBS programs and pilots, and federal and state agencies responsible for delivery of government payments. The purpose of this effort is to improve the distribution of government payments, particularly to those without bank accounts, by exploring various alternatives, sharing information, educating, and assisting in the implementation of programs. In addition, the Management Improvement Fund in the Administration's proposed budget for 1990 has specifically earmarked $12 million for EBS.

ABA is striving to inform bankers and policymakers about these programs. Yesterday, on June 5, 1989, it sponsored a Washington, D.C. symposium on electronic government benefits. That symposium examined EBS pilot systems currently in operation as well as several still in the planning stages. The symposium gave interested parties an opportunity to learn first hand about the EBS programs and possibilities, and to offer suggestions. In addition, ABA included a special session on this subject at its National Operations and Automation Conference held last month, a meeting which drew thousands of bank personnel from the United States as well as overseas.

These programs and pilots represent just a few examples of the current innovations and efforts to promote the distribution of government payments in an easy, safe, and cost-efficient manner. A further listing of some state initiatives is attached to this Appendix.

A legislative mandate to require depository institutions to cash paper government checks for noncustomers would drastically reduce the incentive to advance these new programs and would instead perpetuate a system which is costly and inconvenient to all concerned. It would mandate a system of accessing benefits which would be inferior to methods already in use by federal, state, and local governments, and impose a method which is not the preference of beneficiaries who have had a chance to sample the alternatives.

Mandated Government Check Cashing Would Increase Bank Exposure To Fraudulent Schemes And Current Losses Would Rise Dramatically

While S.906 represents an improvement over earlier proposals, serious problems would remain with regard to fraud potential. Banks are reluctant to cash government checks for noncustomers for very legitimate and serious business reasons. Although there is little doubt that the United States Treasury or any valid government entity will pay properly endorsed, authentic checks, these government checks are not the equivalent of cash. For instance, the Treasury and other units of government will not pay counterfeit checks, checks endorsed by someone other than the payee, or altered checks. This means that the government will not reimburse a bank for a check which was stolen and falsely endorsed or a check on which the amount was altered. Generally, banks today may protect themselves by refusing to cash checks for strangers or checks which they view as false or altered.

While some argue that current losses to banks from uncollectible Treasury checks are low, such statistics are not reliable for gauging the bill's impact. First, they only represent losses from U.S. Treasury checks and do not show losses from state or local government checks. Second, they reflect the losses experienced in an environment in which banks and other check cashers may protect themselves by refusing to cash checks for strangers at their discretion.

To argue that all banks should cash government checks for noncustomers because current losses are at an "acceptable level" is like arguing that polio vaccination should be discontinued because so few cases of the disease are now reported. In both instances, reason suggests that the low incidence is the result of cautionary measures taken and not a justification for dispensing with them. Without those current preventive measures on which banks may choose to rely, losses from fraudulent government checks will increase dramatically.

An example of even a single case demonstrates the ease of fraud and the potential liability under S. 906. Under the bill, a stranger could visit a New York bank and register for government check cashing privileges. Later, the stranger could walk into that branch with proof of registration and with a counterfeit $1,500 check ostensibly drawn on the State of California. The bank, which would have a very limited ability to verify the authenticity of the check, must pay the person $1,500 in cash immediately, even if it reasonably believes that the check is counterfeit. The person could then cash additional $1,500 checks at two more branches of the same bank and then disappear. While the bill limits the amount of a single check eligible for mandatory cashing, it does not restrict the number or aggregate amount of checks which the bank must cash. Thus, losses are potentially quite high.

When the checks later prove to be uncollectible, the bank will likely never recover the money paid out; the person has no account relationship from which the bank may deduct the amount and the individual is not traceable. For small institutions in particular, even a modest sized check would represent a significant loss.

The bill includes three provisions which attempt to limit potential fraud, but these measures are inadequate. First, the legislation allows a bank to reject an application if it discovers an "intentional material misrepresentation." While this may protect a bank if it somehow discovers that individuals have lied about their name or address, it does nothing to screen those who have in the past been involved in check fraud or other related theft activity. Essentially, the applicant's criminal history becomes irrelevant.

Second, the bill provides that services need not be extended to individuals who hold a transaction account or government check cashing relationship at any other depository institution. Presumably, this in part is intended to prevent persons from registering with several banks and cashing unlimited counterfeit or duplicated checks in a number of banks and their branches. However, the protection is somewhat illusory because there is no effective means of enforcement. Without doubt, legitimate customers will willingly abide by the restriction. In contrast, depository institutions cannot rely on check counterfeiters to voluntarily comply. There is no way for a depository institution to ascertain whether an applicant for government check cashing services already maintains other relationships with depository institutions. Thus, if an applicant intends to cash fraudulent checks at numerous institutions, this provision will not hinder that person.

The final provision which attempts to insulate banks from fraud losses allows the Board to suspend any obligation to cash any check belonging to a "classification of checks" which the Board determines is causing unacceptable levels of fraud loss or which the Board has reasonable cause to believe may be used in a fraud scheme. The Board must report to Congress in the event it invokes this provision. Although necessary, this provision will be utilized only in very unusual and unlikely circumstances. Even then, it would be invoked only after substantial losses have been incurred. It is the legislative equivalent of closing the barn door after the herd has been stolen.

In addition to the limited value of these "anti-fraud" measures, the bill fails to include the critically required discretionary right of a depository to decline to cash a check which it believes to be counterfeit or improperly endorsed. Under S.906, a depository institution would be legally required to cash a government check even though it has a reasonable belief that the check is fraudulent! Any legislation which requires depository institutions to cash government checks for noncustomers must allow depository institutions to refuse a check if it has a reasonable belief that the check is fraudulent.

Moreover, such a standard should not be so strict as to be practically unusable.

In order to further reduce the potential for fraud, any legislation should limit the check cashing requirement to U.S. Government checks and should mandate full indemnification to banks which are defrauded while complying with the bill. While the delivery of state and local benefits should properly be left to those levels of government, the federal government should certainly not require a depository to cash a benefit check issued by a state other than the one in which it is located. Under S.906, depository institutions located in Massachusetts would be required to cash checks issued by Hawaii. A Massachusetts teller is likely to be unfamiliar with a Hawaii state check and has no real ability to verify its authenticity. Requiring depository institutions to cash out-of-state government checks does not further the objective of the legislation, but may offer check counterfeiters a welcome opportunity.

Depository Institution Should Not Be Required To Subsidize Government Check Cashing Services

S.906 allows depository institutions to charge customers a fee for cashing a government check so long as it does "not exceed an amount needed to recover all related costs, including fraud losses, as determined by the Board...." While we certainly agree that depository institutions should be permitted to charge a fee for the service, we question whether the Board will be able to establish a fee which fairly represents the costs of depository institutions nationwide. As with many products and services, costs vary greatly from institution to institution and from one geographical area to another. For example, for banks located in urban areas with large populations of government recipients, the costs of staffing overcrowded branches on government payment days may be far greater than for other depository institutions. Because government payments usually arrive on the same day for all recipients, branch overcrowding on payment days can severely strain the depository institutions' resources as well as create inconveniences for its regular customers, including local businesses. And, we can expect that losses attributable to fraud will vary markedly from institution to institution. An amount established by the Board based on "average" costs simply will not adequately compensate many banks for the costs of providing the service. These institutions will then be compelled to subsidize the service. This additional expense will not be borne by nonbank competitors.

Instead, any legislation mandating government check cashing should allow depository institutions to charge a "reasonable fee" determined by each depository institutions, subject to Board review. Such a provision would ensure that only appropriate fees are charged but would fairly accommodate the variations in depository institutions' costs.

Absorbing the Cost Of Government Check Cashing Would Threaten The Viability Of Marginally Profitable Branches, Particularly Those Located In Low Income Areas

The additional expenses incurred by those depository institutions whose actual costs exceed the regulatory limit will most significantly affect those branches which are located in low-income areas where demand can be expected to be high and which may already operate at a loss or only marginal profitability. The anticipated volume of demand and consequential costs may force banks to close some of these branches. In addition, banks may hesitate to open new branches in low-income neighborhoods due to the burden of providing these services. Minority bankers have expressed a particular concern about such requirements. Thus, rather than assisting those living in low-income areas as the bill intends, the availability of financial services may decline for many low-income Americans.

MANDATED BASIC BANK ACCOUNTS

As stated earlier, ABA endorses the concept of basic banking and believes that banks should endeavor to design products which respond to the particular demands and needs of their potential basic bank customers on an unsubsidized basis. In 1985 we took the lead in urging our banks to provide low cost checking in their communities. We have found that banks have responded very positively as shown by the significant increase in the availability of basic bank accounts in recent years. Our surveys show that in 1986, 47 percent of banks had basic bank accounts. Since then, the percentage has increased to 53 percent with an additional 8 percent of banks planning to offer them.

We believe that, given the wide and growing availability of basic bank accounts, a legislative mandate is unnecessary. Furthermore, a single statutorily defined basic bank account cannot be expected to respond to the needs and demands of all potential basic bank account customers. Different groups will prefer different features. A rigid statutory account will stifle the introduction of more imaginative products which better meet potential customer preferences.

S.907 requires depository institutions to offer a checking account which assesses a service fee not to exceed the amounts set by the Board based on studies of actual costs. The account must permit at least ten withdrawals per month and allow check transactions. No minimum opening or maintenance balance may exceed $25. The account must allow direct deposit of recurring payments. To register for an account, an applicant may be required to present a photo identification. A depository institution may reject a registration if it determines that an "intentional material misrepresentation" has been made in the information provided.

Basic Bank Accounts Are Already Widely Available

A large number of banks currently provide basic bank accounts. An ABA survey conducted in 1988 shows that 61 percent of banks either offer or plan to offer a basic bank account.

A closer look at the survey reveals that a much higher percentage of the largest banks (those with more than $1 billion in assets) offer such accounts. In fact, as the table shows, over 73 percent of the largest banks voluntarily provide low cost transaction accounts and an additional 14 percent plan to introduce such an account. This is significant because these larger banks tend to serve urban populations whose need for low cost financial services is the greatest.

	Asset Size (In Million Dollars)				
	Less Than 50	50-100	100-500	500-1,000	1,000 or More
Banks Offering	51.0%	47.2%	61.5%	70.9%	73.8%
Banks Planning to Offer	2.9%	8.8	9.7	7.4	13.8

* Basic bank account is defined as an account that offers limited banking services to the general public at no cost or reduced cost. Typically, minimum balance requirements for these plans are low or nonexistent, and debit transactions and/or the number of checks written are completely free or free up to a minimum.

A recent survey conducted by the New York Banking Department reached similar conclusions regarding the widespread availability of basic bank accounts in that state. It found that in each of the New York State's ten metropolitan regions there are depository institutions offering basic bank accounts which, based on 6-10 checks per month, require $100.00 or less to open, and charge $1.00 or less per month in service fees. A significantly larger number of depository institutions offer such accounts with service fees ranging from $2.00 to $4.00. The survey also found:

- o on average the minimum balance required to open a checking or savings account was less than $25.00;
- o about one quarter of institutions imposed no monthly fee on checking accounts;
- o of those that impose a monthly fee, a substantial majority do so only if the required balance is not maintained.

The survey was based on responses from 97 percent of all state and federally chartered commercial banks offering retail services and all state and federally chartered savings and loans and state chartered credit unions. The study concluded that there is a "widespread availability of low cost banking services through New York State."

Banks in other areas have demonstrated commitment to providing basic banking services. For example, in 1987, nine Philadelphia area banks said they would offer low-cost accounts as part of an agreement with metropolitan area neighborhood groups.

Particular concerns have been raised regarding the availability of basic bank accounts for older Americans. A 1988 survey conducted by Sheshunoff & Co. indicates that 78 percent of banks provide free checking to senior citizens. An additional 3 percent offer discounted checking services to seniors.

Studies show that a large segment of the population maintain at least one checking or savings account. The April 1987 *Federal Reserve Board Bulletin* reported that in 1983, about 88% of households surveyed held either a savings or checking account. Similarly, the Board's 1986 Survey of Consumer Finances found that 89.2% of those surveyed had a checking or savings account. A 1988 national survey by SRI Research and *Bank Advertising News* found that 87% of Americans said they had at least one checking account. This number does not include those people who do not maintain a checking account, but do have another bank account such as a savings or money market account.

In the last Congress, in its discussion of the reasons for mandating basic bank accounts, the House Banking Committee Report to H.R. 5094 cited estimates that nearly 20 percent of families maintain no bank account relationship. However, the April 1987 *Federal Reserve Bulletin* reported that in 1983, while about 21 percent of families surveyed had no checking account, only about 12 percent of the households surveyed held *neither* a checking nor a savings account. Thus, eight in nine American households now have the ability to have government benefits electronically deposited and/or cash government checks.

A mandatory Federal solution to the difficulty of reaching that remaining one-ninth of households will stifle innovation and will not be sensitive to local circumstances. The banking industry wants to work with you in reaching out to this unserved population. But flexibility must be granted, and a common goal for defining success is needed, as sociological barriers and personal choices will prevent us from ever having one hundred percent of households maintain a depository relationship in the real world where we compete.

One Uniform Basic Bank Account Will Not Respond to the Needs of All the Individual Markets and Will Inhibit Development of More Responsive Accounts

The proposed legislation mandates very specific features for basic bank accounts. Such a rigid delineation inhibits initiatives to offer basic bank accounts which may not fall within the parameters of the statutorily defined account, but which in fact reflect the preferences of those local households interested in basic banking accounts. For example, individuals in one segment of the market may be willing to accept a higher minimum balance or fewer permitted transactions per month in exchange for lower service fees. Others may prefer direct deposit of recurring payments if there is no minimum or maximum balance requirement.

It is difficult to determine which characteristics are most desirable or useful to those interested in a basic bank account. Currently, because many banks offer some type of basic bank account, customers may select the account which best suits their needs. Allowing the market to define the basic bank account will help to assure that the greatest number of people are accommodated. One mandated account will greatly limit alternatives because banks are highly unlikely to offer more than one type of basic banking account. Such innovations should be encouraged, not inhibited by a legislative mandate.

Many of the accounts available today demonstrate imagination and innovation in responding to customers' preferences. For example, the First National Bank in Albuquerque developed a basic bank account based on its market research. The resulting account assesses no maintenance or transaction fee nor any minimum or maximum balance requirement. Customers may choose to pay an additional $2.00 per month for overdraft protection. For an additional dollar, they may buy unlimited local movie theatre tickets for half price, an option that has proven popular.

The features of the account respond to the bank's market research which concluded that fear of overdrawing an account and affordability of discretionary items such as entertainment were top concerns for many local individuals. The account has been marketed by bank representatives speaking in factories, department stores, and other companies. It is very popular, particularly among blue collar workers.

Legislation Such As S.907 Does Not Adequately Protect Depository Institutions Against Fraud

One of the most disturbing aspects of mandating basic bank accounts without allowing depository institutions the discretion to deny or close accounts is the inevitable fraud that could result from mandatory availability. For example, under S. 907, virtually anyone may insist on an account regardless of their financial history.

The safeguards included in S.907 which are intended to protect depository institutions from fraud or financial mismanagement do not adequately shield banks. For instance, while the bill allows a depository institutions to reject an applicant if it finds an "intentional material misrepresentation," the bill lacks any provisions to enable a depository institution to reject based on knowledge that the applicant in the past has mismanaged or abused an account or even defrauded an institution. The inability to reject an applicant on the basis of prior fraud or mismanagement is especially worrisome in light of the recent funds availability law requiring depository institutions to release funds before they know them to be collectible. Multiple accounts and unfettered access to funds present an attractive combination to organized crime.

It would be extremely difficult to translate a standard for reasonable denial of an account into statutory language which avoided being too vague or too rigid. Again, unless the federal government is willing to indemnify against all potential losses, depository institutions must be permitted fairly broad discretion regarding those with whom they will commence an account relationship.

Mandated Basic Bank Accounts May Unfairly Impose Costs On Banks

As we have already stated, ABA encourages banks to offer basic bank accounts designed to respond to local needs. However, such products should not be expected to lose money. If depository institutions are required to offer accounts whose charges do not cover costs, they will need to charge higher loan rates and fees on other services, and pay lower interest rates on savings products than those offered by credit unions and other nonbank competitors. For these reasons, some bank customers may shift to financial service providers who are not subject to this bill. We must ask why these other providers should not also be asked to offer basic accounts if they provide transaction account services generally.

While S. 907 permits the Federal Reserve Board to set permissible fees based on studies of actual costs, we do not believe that the Board is capable of calculating a fee which will fairly represent costs for all depository institutions. As we explained earlier with regard to determining the costs of government check cashing, costs may vary dramatically from institution to institution. Because different institutions will encounter different levels of account demand and different expenses for providing the accounts, a prescribed fee based on "average" costs will not ensure that a depository institution recovers its costs. The rate setting burden which would be imposed on the Board should not be underestimated.

Absorbing the Costs of Basic Bank Services Would Threaten the Viability of Many Branches, Particularly Those in Low Income Areas

The additional costs of providing basic bank accounts, particularly in conjunction with a government check cashing service, will most significantly affect those branches located in low-income neighborhoods which already operate at a loss or are only marginally profitable. Because demand for the basic bank accounts and government check cashing services could be particularly strong in these areas the extra costs of the services, including fraud and mismanagement losses, may force depository institutions to close some of these branches. Furthermore, depository institutions may hesitate to open new branches in low-income neighborhoods due to the burden of providing these services. Thus, the effect of providing basic banking and government check cashing services as mandated by the bill may make financial services less available in low and moderate income neighborhoods.

A May 1988 study conducted by Booz Allen & Hamilton, Inc. concluded that about half of the nation's branches are unprofitable or only marginally profitable. The report indicates that achieving profitability is more difficult for small banks which lack certain economies of scale. More branch closings and fewer branch openings, especially in low-income areas, will likely result from placing additional mandatory burdens on community banks as well as many branches of larger banks.

COMMUNITY REINVESTMENT ACT

ABA Supports Community Reinvestment

Mr. Chairman, the members of the American Bankers Association support both the spirit and the intent of the Community Reinvestment Act. We recognize our responsibility to serve the financial needs of our local communities, and we do not condone discriminatory practices in the provision of either deposit or credit services.

In our remaining testimony, we fully address the scope of issues raised by your questions dealing with CRA. Let me just briefly summarize our response.

First, you ask whether the focus of CRA should be shifted from the application stage to the CRA examination. The best results for both the community and the bank will come from open dialogue among all interested parties. Community involvement should not be considered a confrontational event -- it should be an ongoing process of cooperation to identify community needs and find ways to satisfy those needs. In other words, CRA should strive to establish a solid working relationship between community groups, banks and regulators, in which differences are first illuminated and then resolved. The present administration of CRA is generally working in this way, despite a few well-publicized confrontations triggered by specific applications. Shifting emphasis to the examination -- that is, shifting the timing of initiation of government sanctions against the bank to a below-par exam rating -- would eliminate the time period between evaluation and application in which accommodation can now be reached. It would shift attention from the institution's response to the exam to the exam grade itself. It could lead to both the bank and community groups seeking to unduly influence the examiner, and place the examiner in the inappropriate position of being asked to mediate disputes, diverting proper attention from impartial fact-finding.

Your second question asks how to encourage successful CRA programs. We believe that successful CRA stories are becoming common around the country -- my full written statement outlines a handful of such stories, and others testifying before the subcommittee tomorrow will discuss many more. The key to success is clear -- cooperation and communication between community groups and banks. We want to work with the Congress in helping to disseminate these success stories to other banks and community groups, so that they may be replicated and expanded. Also, consideration should be given to whether the banking agencies can be involved in such an effort, as well as whether other agencies of government can get involved -- perhaps through "seed money" or technical assistance -- in catalyzing community-based housing, health, and social service projects.

Your last question deals with the benefits and problems of disclosing ratings and examination reports to the public. Disclosure seems simple enough -- but, again, it results in shifting the spotlight from the application stage to the examination stage. We believe CRA is working well, and that such a fundamental change is therefore unnecessary. It will not foster better relations nor better understanding between banks and community groups. It will make the examination process a confrontational event, and could lead to examiners shading their opinions instead of being impartial fact-finders. Also, since the exam process involves nonquantative evaluations, a simplistic comparison of rating numbers between banks in different regions and circumstances could lead to incorrect assumptions about their relative commitments to their communities. Based on our conviction that cooperation is more productive than confrontation, we support the approach recently taken by the regulators in the joint policy statement on CRA. These new regulatory guidelines should be given an opportunity to prove their merit before any changes are made in the CRA statute itself.

Cooperation Preferable to Confrontation

These oversight hearings are very important. We believe that the testimony before this Subcommittee will show that banks have made substantial progress in community reinvestment. Moreover, we believe that the framework recently established by the bank regulators to guide CRA compliance will continue to foster improved cooperation between banks and community groups. We look forward to working with this Subcommittee, the regulators, and community groups to ensure that the Community Reinvestment Act meets its objectives.

We are concerned, however, that the growing trend toward cooperation between banks and community groups may be threatened by unnecessary changes in the CRA statute. There have been proposals in both the Senate and the House to amend CRA to require public disclosure of examiner evaluations and ratings of a bank's CRA performance. The proponents of legislation such as S. 909 portray it as a simple disclosure. In reality, it is not so simple. In fact, we believe that disclosure of examination ratings and evaluations will change the nature of the CRA examination process, and will complicate CRA enforcement rather than improve it.

The intent of the proposed legislation is to create greater bank sensitivity to community needs, but the result is likely to be just the opposite -- it will discourage dialogue and increase confrontation. Right now, the bank regulatory agencies are encouraging interested parties to comment on banks' performance on a continuing basis, allowing banks and community leaders to work out acceptable solutions prior to CRA examinations. Publicly disclosing examiner ratings and evaluations will discourage this blossoming dialogue between community groups and banks by turning the spotlight on the results of the CRA exam. Banks and community groups will direct more time and attention to building a record which justifies past practices -- looking toward influencing the the exam finding -- than they will devote to finding a common ground of agreement and objectives.

In addition, exposing the full scope of CRA exams and evaluations to public view will inhibit candor in examination staff communications to the agencies, making supervision and examination more difficult. If examiners expect their findings to be publicly disclosed, they are more likely to moderate their comments, eroding the overall effectiveness of the examination process.

The remainder of my statement on CRA this morning is divided into two sections. First, I would like to focus on the CRA statute itself -- the elements of a good CRA statute, the contributions CRA can and cannot be expected to make to a community's well-being, and which financial institutions should be covered by CRA. And second, I would like to briefly discuss a few specific examples of the types of CRA programs banks across the country are undertaking, and to describe what the American Bankers Association is doing to help our member banks develop CRA programs which are good for both the community and the bank.

Elements of a Good CRA Statute

During the course of these hearings, you will learn in some detail about community lending programs designed and administered by banks in many communities. One thing that will become obvious is that each CRA program is tailored to meet the needs of the community in which the bank operates. This may seem like a trivial, perhaps even unimportant observation -- but in fact, it is critically important. Not every community has the same credit needs -- so a good community reinvestment statute must be flexible. Obviously, a community in rural Texas does not have the same needs as Chicago.

To be successful, a community reinvestment statute must engender cooperation between the community and the bank. Mr. Chairman, we have just had an example in your home state of Illinois which demonstrates just how far CRA has come in encouraging such cooperation. The major banks in Chicago have just launched the largest community reinvestment effort in the country -- not as a result of confrontation over a CRA examination or an application subject to CRA protest, but as a result of constructive dialogue between the banks and the community.

Finally, an effective community reinvestment statute should clearly define the responsibilities of both the community and the bank. Just as bankers must be responsive to the credit needs of the community, community groups must use their expertise to help define local credit needs and must be willing to work with the bank on an ongoing basis to find responsible ways for banks to meet these needs within the parameters of safe and sound operation.

In short, the ideal community reinvestment statute will be flexible enough to recognize differences in community credit needs, will encourage dialogue and cooperation between banks and community groups, and will clearly define the responsibilities of both banks and community groups in the CRA process. The ideal statute should not amount to credit allocation; divert necessary time of examiners from their safety and soundness function; or be a source of confrontation between banks, community groups, and regulators.

CRA Cannot Solve All Community Problems

While a good CRA statute can contribute to a community's vitality, it is important to recognize what CRA cannot accomplish. No matter how good the CRA statute is, it is simply naive to believe that the economic ills of our cities, towns and rural areas will magically be cured by requiring banks to supply credit to low and moderate income communities. And, of course, it would be fundamentally unsound to require banks to lend funds for purposes that were not creditworthy, no matter how worthwhile.

Decreases in federal expenditures for low-income housing and community revitalization, cut-backs in federal small business loan guarantees, and declines in mass transit, job training, and primary and secondary education spending levels have undoubtedly had a significant impact on the vitality of low-income communities. Also to be considered are broader demographic factors affecting community conditions, particularly in terms of effect on housing stock and demand for public services.

In other words, the economic deterioration often witnessed in inner city neighborhoods and rural areas reflects a broad array of problems resulting from a variety of interrelated factors. The availability of credit is only one part of the complex process of community growth, decline, and rebirth. In this dynamic process, the lack of bank credit is not the sole or even the principal reason for neighborhood deterioration -- nor will increasing the availability of bank credit be a panacea.

Other Financial Service Providers Should Be Covered By CRA

Another very important consideration is that banks are not the only financial institutions receiving household and business savings dollars for reinvestment. Money market funds and mutual funds actively solicit both business and consumer funds, drawing billions of dollars out of communities across the country -- but they have no CRA responsibility. Credit unions are attracting an increasing share of savings/investment dollars. But credit unions, even those with community charters, are not subject to the CRA statute. Insurance companies market many savings and investment products, and their assets are virtually indistinguishable from banks', yet they have no CRA to comply with when they lend.

This Committee is well aware of the many inroads that nonbank competitors are continuing to make against commercial banks on both the asset and liability side of the ledger. More recently, we have seen the newer phenomenon of federally-insured deposit institutions soliciting funds nationwide, through mail or other means, which would otherwise reside in local institutions. Unlike some major commercial banks which also gather funds widely, these new institutions have little or no relationship with even the community in which they are located. They also often provide a narrow range of products and services inapplicable to the needs of low-income individuals.

The dollars which are sent to Sears' Greenwood Trust in Delaware will not be available for a small business loan in Detroit or new housing in Boston. Does Sears have a CRA obligation beyond making Discover cards available on a wide basis? And what about the American Association of Retired Person's (AARP) credit union, whose only common bond is a family member aged 50 or older? AARP generally endorses every new proposed "consumer" mandate for banks, yet the elderly will look long and hard for a local AARP branch to cash their Social Security check. Then there is American Express' Boston Safe Deposit and Trust, which advertises that its services are for the "privileged client" with high net worth? What is the "community" that such institutions should serve and do they have a broader obligation to promote services to persons outside the target groups they select for marketing? Commercial bankers would like to know what is expected of these competitors, who have so successfully attracted funds away from our communities and from some of our most profitable customers, before we are asked to offer additional mandatory services and adhere to even higher standards. This is not a matter of sour grapes -- it's a matter of fundamental fairness and of shared obligations to society.

The fact is that banks are receiving a declining share of total private savings funds. Of the total volume of savings dollars flowing out of cities, towns and rural communities and needing to be reinvested, only 35 percent now flows into banks. In the early years of this decade, banks received about 40 percent.

Banking's role in providing credit is also decreasing. The market share of financial assets -- investments and loans to individuals, business, and governments -- held by banks has declined steadily over the past 15 years, falling from 40 percent in 1974 to 29 percent by 1988. The share held by insurance companies, finance companies, mutual funds, securities firms and other non-depository financial firms climbed to 51 percent over the same time period. But none of these other financial service providers are covered by the Community Reinvestment Act.

These trends have important implications for community reinvestment. If banks alone are required to carry the burden of CRA and other consumer/community responsibilities, they will continue to operate at a competitive disadvantage, and will continue to lose market share. And as the relative importance of the banking industry declines vis-a-vis other financial service providers, banks will be less and less able to meet the credit needs of their communities

Regulators' New Compliance Guidelines For CRA

The federal banking regulatory agencies recently issued expanded CRA compliance guidelines. These expanded guidelines will put additional burdens on the banking industry, but they will also increase the effectiveness of CRA and give bankers clearer guidance as to their responsibilities. This clearer guidance should be a plus for all sides. The joint CRA policy statement reflects careful thought by the agencies on how to best achieve the goals of CRA. It offers a balanced approach to community involvement in the CRA process -- one which meets each of the criteria discussed above as elements of a good CRA statute.

The new guidelines explicitly acknowledge that community credit needs vary considerably. Programs which may be well suited to an inner city will probably not meet the requirements of a suburban neighborhood or a small rural area. This is a major concern, especially for our community bankers. We are pleased therefore that the guidelines provide considerable leeway for banks to meet CRA objectives based on the credit needs of their particular community and on each bank's area of expertise. By this same reasoning, the new guidelines broaden the CRA base from its current narrow focus on housing to include business, agriculture, education, and state and local government financing. Again, our member bankers support this more open concept of CRA.

The regulators' guidelines clearly intend to shift the focus of CRA away from confrontation by encouraging consumer/community groups to monitor and comment on a bank's performance on an ongoing basis. Banks and community leaders are expected to work together to establish what the community's credit needs actually are, and to develop programs to satisfy these needs. Cooperation is the key to a good community reinvestment program: we are convinced that the long-term interests of the community will be better served by a constructive interchange of ideas than by the adversarial protest process that has characterized some CRA disputes.

The new CRA guidelines will also improve the consistency of the administration of CRA by applying the same standards to all covered institutions. In the past, different standards were applied by different regulators, achieving uneven results in some cases and making compliance more difficult. This lack of administrative consistency was a concern among our bankers, and we are pleased that the agencies have taken steps to address the problem.

The guidelines also take a big step forward by clarifying the responsibilities of all parties involved in CRA -- banks and community groups alike -- making CRA more effective and making compliance easier. This is a major improvement in the administration of CRA. It is very important that the CRA burden not be placed entirely on the banks; the community must recognize that it also has a responsibility in the process. Community groups must act in good faith to help determine the community's credit needs, and to work with the bank to develop a responsible program to address those needs.

The guidelines are not just cheap talk -- the federal regulators are taking actions based on them. In refusing an application early this year from a major bank holding company for the acquisition of a depository institution in another state, the Federal Reserve Board cited deficiencies in the bank's CRA record. This decision is a clear indication that the regulators are taking a tough stance on CRA compliance.

In sum, we believe the regulators have made major strides in the enforcement of CRA. We support their efforts to improve the workability of the statute and to encourage constructive dialogue between bankers and community groups. Before changes are made in the statute, these new policies should be given an opportunity to prove their merit.

Bankers Are Doing Their Share

The regulators are not the only ones taking CRA seriously. The banking industry has also been working hard in their communities to improve their CRA performance. The banking industry has a strong stake in community health and welfare -- the profitability of each bank is inexorably linked to the vitality of its local economy. The industry therefore has a vital interest in strengthening and diversifying the economic base of the big cities, small towns, and rural areas across America.

In other words, community reinvestment is part and parcel of each bank's livelihood. We believe the vast majority of banks in this country are doing a good job of serving the deposit and credit needs of their communities -- including the needs of low and moderate income areas. Here are a few examples that will help to illustrate banking's commitment to community lending.

Atlanta

In testimony before the full Senate Banking Committee last year ABA's President Tom Rideout presented an extensive discussion of the programs his institution, First Union National, Atlanta, has undertaken in the Atlanta market. This was especially timely because of some negative publicity concerning depository institutions in Atlanta. The most recent step taken by the bank to help the community grow and prosper is a new partnership between First Union and a federal agency to increase lending to minority owned businesses. The bank's partnership agreement with the Minority Business Development Agency is the first of its kind for a major financial institution. Under the program, minority businesses can borrow a minimum of $50,000 at competitive lending rates. The main thrust of the program to to help minorities compete for loans.

Philadelphia

Philadelphia has one of the oldest low-income lending success stories in the country. The Philadelphia Mortgage Plan was created in the early 1970s as a cooperative effort between local banks and neighborhood groups. It has resulted in more than 11,000 mortgage loans to low and moderate income residents. Each participating bank makes and holds its own loans, enabling them to be flexible if the borrower experiences payback problems. Philadelphia banks also participate in the Philadelphia Rehabilitation Program, which is designed to provide for renovation and rehabilitation of housing units.

A small business loan program in Philadelphia has generated at least 1,000 additional jobs in the Philadelphia market. The lending focus is primarily on small entrepreneurial activities in neighborhoods which will help to promote employment in these areas. Each of these programs are excellent examples of how lenders and community groups can develop an effective lending program out of common goals and concerns.

Chicago

Chicago provides another clear example of banks' commitment to community lending. Last month, First Chicago announced that it will make $150 million available over the next five years for residential and small business loans in low and moderate income Chicago neighborhoods. This program is not connected to an acquisition application by any of the participating banks. It came about from bankers and community lenders working together over an extended period of time, as CRA intended.

Two other large Chicago banks, Harris Trust and Savings, and Northern Trust Company, have also announced a renewal of their agreements to lend a total of $75 million in low-income areas during the next five years.

Minneapolis/St. Paul

In Minneapolis/St. Paul, First Bank System is involved in a major public/private partnership to meet the need for affordable housing in the Twin Cities. First Bank System, together with other corporations, has formed the Metropolitan Low Income Neighborhood Housing Partnership to encourage local businesses to invest in low-income housing. The members of the partnership have contributed a total of $10.5 million which is available to developers of multi-family housing projects for low-income residents. First Bank System provides additional expertise by acting as a managing partner.

Boston

For Boston Bank of Commerce, community reinvestment has been a winning business strategy in a highly competitive marketplace. The bank is actively involved in Boston's Parcel to Parcel Linkage Program, an innovative program designed to stimulate neighborhood growth. Using the bank's network of minority businesses and community leaders and organizations, a development team was established that is initiating projects to attract new jobs to Roxbury and provide funding for development of affordable housing, child care facilities and job training.

St.Louis

Boatmen's National Bank of St. Louis has loaned over $102 million for one to four family residences and multi-family residential buildings in low and moderate income areas. In addition, the bank has announced a neighborhood partnership program through which the bank makes $100,000 available annually for grants to local neighborhood organizations. These neighborhood groups are the backbone of Boatmen's community reinvestment program. The bank continues to reach out and maintain a constant dialogue with neighborhood organizations as well as city, county and state housing officials.

These examples are just that, examples. Banks and community leaders across the country are working together on similar projects dedicated to low-income housing and business lending.

ABA Is Actively Helping The Industry's Community Reinvestment Efforts

One of the priorities established by ABA's Board of Directors involves the issue of consumer and community compliance. The ABA and its member banks understand the importance of these matters and want to work with members of Congress to address them. To maintain progress on this, ABA President Tom Rideout last year appointed a Community Involvement/Consumer Compliance Task Force consisting of bankers representing a wide size and geographical range. The mission of the Task Force is to identify the key consumer/community issues and to make recommendations to the Board on how ABA can help its member banks establish sound working relationships with community groups in their market areas, and to help develop programs which satisfy the needs of both the community and the bank.

Frankly, one of the greatest strengths of this Task Force is in the sharing of information and expertise on community issues among bankers. While all communities have their own special needs, there are clearly lessons which can be shared on how to approach problems and how to design appropriate bank programs. Among the greatest accomplishments of the Task Force is the increased visibility of community issues among top level bank managers -- and, as you will hear from each of the bank witnesses on CRA, a successful bank community lending program requires the support of top management.

A key focus of the Task Force is to develop educational tools to help bankers develop effective CRA programs. In response, our Housing and Real Estate Finance Division has created a new subcommittee of real estate lenders who specialize in low-income housing and community development lending. The subcommittee's major goal is to shape and support a new banking specialist -- the community development lender. In effect, we have set up a mini-trade association within ABA to encourage banker development and bank involvement.

ABA's Housing and Real Estate Finance Subcommittee will focus its attention on affordable housing for low and moderate income families, transitional housing, and other community-based facilities, as well as the financing methods for these products. The mission statement of the subcommittee includes the following:

- Promote through information and specific actions community development lending as a wholesale banking line;

- Shape and support a new bank specialist -- the community development lender;
- Identify the business opportunities in community development lending;
- Expedite the involvement of corporate America in the solution of the housing problem, especially enlisting other financial service entities;
- Participate in the development of public policy and legislative issues affecting community development;
- Work toward the formation of specific programs involving transitional and affordable housing on a national level and in conjunction with other institutional lenders, national organizations and industry trade associations;
- Work on expanding the capability of the secondary market to deal with the funding and securitization issues of affordable housing.

A final project meriting mention initiated by the ABA Task Force is the development of a software package which will help banks compile the documentation necessary to comply with the new CRA guidelines. This software program will offer bankers a simple and organized way to document and present CRA information.

Conclusion

Bankers are working hard to strengthen their community involvement. The examples presented in this statement illustrate the variety of creative programs designed by banks in cooperation with community groups, programs which are improving the quality of life in towns and cities across the country. It needs to be emphasized that the handful of programs cited here this morning are merely examples -- these and other innovative approaches to community problems are being repeated over and over again industrywide.

Mr. Chairman, as shown by these examples, America's bankers are anxious to develop programs to help solve the problems of the less fortunate in our society. In addition, we stand ready and willing to work with the members of this Committee and others in the Congress to develop additional and viable solutions. First and foremost, we want to work with you to make sure that there is absolutely no discrimination in lending by any American business organization.

The answers are not simple. We must be careful to craft workable solutions -- solutions which are not counterproductive and which do not impose unnecessary cost burdens. There are a number of considerations to be taken and questions to be answered. Among them are:

1. We must design programs which are fair and equitable among providers of financial services. Certainly, there is no part of the financial services industry that serves its communities more directly than banks. Yet, banks are now, in most categories, providing less than

a majority of financial services. For example, insurance companies are providing savings-like products, and securities firms have taken hundreds of billions of dollars into money market funds and other types of mutual funds which traditionally went to the banking industry. Should not they be subject to equivalent requirements with respect to reinvestment? If not, won't they continue to have cost advantages which benefit them at the expense of the banking industry, further exacerbating community reinvestment concerns?

Another example would be credit unions. Should not credit unions, with the tremendous expansion of the common bond concept, be subject to the same requirements as banks? In particular, how can one justify excluding credit unions which have a given community as their common bond from requirements with respect to reinvestment in that community?

2. How can we minimize the regulatory cost burden on the banking industry? Our industry is already straining under a tremendous load of regulation. It was ironic to hear a Senator claim in a recent Senate floor debate that this Banking Committee had done little recently to help consumers. What was the Funds Availability law enacted in last Congress, a law which generated a regulation and supporting documents of 600 pages? What was the Credit and Charge Card Disclosure Act, an innovative piece of legislation which the banking industry supported? What was the Home Equity Disclosure Act, where once again the industry worked cooperatively with you? It seems to me that this Committee has a strong record on consumer legislation. But these laws, and literally dozens of others which have been enacted in recent years, have put a huge burden on our industry, a burden which will only be exacerbated by the savings and loan legislation about to be enacted. As our cost burdens increase, our competitive position deteriorates; and as our competitive position deteriorates, other providers of financial services who are not required to serve their communities will take a larger slice of the market. This must be taken into account in designing solutions to the problems we face. Where real problems exist that are not being adequately addressed through local efforts, both public and private, then perhaps federal legislation is in order. But bankers want some assurance that the standards set for them are equitable and stable, and that they do not face the prospect of a never-ending stream of new legislative "solutions" in search of alleged problems.

3. How can we avoid designing federal legislative solutions which will have the counterproductive impact of inhibiting or even stopping innovation at the state and local levels? As outlined in our testimony, banks, local governments, and consumer and community groups are working together to design innovative solutions which meet the particular needs of their communities. We must be very careful not to order a federal solution which will end these initiatives. After all, all wisdom does not reside within the Capital Beltway, and we should all be anxious to encourage innovative solutions which can serve as examples, rather than mandating a rigid process that will stifle them. Perhaps the Committee should be giving consideration to cooperative measures which will survey the many approaches underway, disseminate information to the financial community, and spur pilot programs to test new approaches or technologies.

4. How can we work together to design solutions which are applicable in all of the diverse communities throughout this country? In a recent meeting of our Government Relations Council, the questions was raised as to how laws designed to deal with Chicago or New Haven could apply to a small agricultural community. We must remember that thousands of banks throughout this country are, in fact, very small businesses. If you design a program in Washington targeted at large banks in urban areas, how can that be applicable to a small bank in an agricultural community? Is it a correct public policy to force such institutions to design programs, or to institute new types of accounts, which will have a large cost relative to the size of the institution and which may, in fact, seldom or never be used? Just as an example, most community banks throughout this country cash government checks for anyone who walks in the door, so long as that person has proper identification. It is right for them to be required to set up a new program for cashing government checks, a program which will be very expensive relative to the size of a small bank, when such a program will almost certainly never be used?

These are just some of the questions that we must grapple with in designing programs to deal with the issues before us. Mr. Chairman, the ABA is anxious to work with you and the members of this Committee toward a solution to the problems raised by this hearing, just as we have increased our dialogue with the regulators.

The regulatory agencies charged with implementing the CRA statute are devoting increased time and resources to establishing a workable uniform framework which will encourage cooperation among all interested parties and will provide the flexibility necessary to ensure that each community can have a CRA program tailored to its own individual needs. Recent regulatory actions clearly show that the regulators will not hesitate to cite noncompliance with CRA in refusing applications for acquisition by depository institutions.

In brief, both the banking industry and bank regulators are committed to seeing that the spirit and intent of the Community Reinvestment Act are realized. Great strides are being made to achieve this goal. The Community Reinvestment Act is working and even being reinvigorated. Bankers and community and consumer leaders are working on innovative programs across the country to attain the goals of this important statute.

I appreciate the opportunity to represent the ABA before the Subcommittee and would be pleased to answer any questions.

APPENDIX

THE FOLLOWING STATES AND LOCALITIES HAVE ESTABLISHED OR ARE PLANNING TO ESTABLISH WORKING ARRANGEMENTS WITH BANKS OR OTHERS TO HANDLE DELIVERY AND/OR CASHING OF GOVERNMENT CHECKS

PENNSYLVANIA:

- The department of welfare has contracted with the largest commercial banks in the Philadelphia and Pittsburgh market areas for direct delivery of welfare checks (not electronic funds delivery) and food stamps.
- Bank participation is voluntary.
- Welfare checks and food stamp authorizations are delivered by mail directly to participating banks according to zip code; the volume to be handled by each bank is arranged among participating banks in each area.
- Recipients are issued a photo ID by the state which is presented to the appropriate bank to either claim/cash their welfare check or receive their food stamps.
- The banks are indemnified against loss in cashing welfare checks provided that they follow proper procedures regarding IDs and endorsements.
- Participating banks receive a fee from the state for their services.
- The driving force behind the development of this program was to reduce fraud rather than the inability of recipients to cash welfare checks.

NEW YORK CITY:

- The Human Resources Agency of New York City has contracted with Manufacturers Hanover and several New York check cashers to distribute welfare funds and food stamps to recipients.
- The city provides each participating M-H branch and check cashing facility with hardware for the electronic delivery of welfare funds and food stamp entitlements.
- The city issues recipients a photo ID with a magnetic strip containing information on the amount of funds and/or food stamps to which the recipient is entitled.
- The city pays participating institutions a fee per transaction.
- The driving force behind this program was to reduce fraud; reports indicate that it has achieved this goal.

OHIO:

- Summit County (which includes Akron and Canton) has established a voluntary pilot program for the cashing of public assistance checks.
- The county is responsible for issuing an ID card to recipients.
- Each recipient selects a depository institution at which they wish to cash their check (up to three locations may be selected, not necessarily of the same institution) and the county supplies each institution with a copy of the ID card.
- The institution does not charge the recipient for cashing the check.
- There is no indemnification for fraud losses.

MINNESOTA:

- The Ramsey County Community Human Services Department designed a pilot program for electronic delivery of public assistance payments.
- A random sample of about 1,000 AFDC and refugee assistance recipients was selected to participate in the pilot project.
- Participating recipients are issued picture ID cards with magnetic strips encoded with the benefits to which they were entitled.
- Participants can withdraw some or all of their benefits at selected ATMs and/or operator assisted teller machines.

NEW JERSEY:

- The state will mandate EBS for Aid to Families with Dependent Children payments and food stamps in the three most populous counties starting January 1990.

THE FOLLOWING STATES HAVE ENACTED LAWS DEALING WITH CASHING OF GOVERNMENT CHECKS

CONNECTICUT:

- Applies to all banks, industrial banks, and savings and loans. Credit unions are only required to cash checks for their members.
- Each institution must cash state-issued public assistance checks provided that the check is presented by the payee and that the payee has "reasonable" identification. The State Banking Commissioner and the Commissioner of Income Maintenance are currently writing the regulations regarding what constitutes "reasonable" ID.
- The depository institution may not charge the payee for cashing the check, but may request a fee from the state for cashing such checks.
- The state will indemnify the depository institution from loss on checks cashed provided that the institution follows identification procedures established by the state.

MASSACHUSETTS:

- Requires banks and thrifts to offer free checking and savings accounts to residents over 65 and under 18 years old.
- Requires banks and thrifts to cash federal, state and local government retirement, social security and supplemental security income for checks for residents provided the payee is registered with the institution.
- Each branch bank or thrift must offer registration for resident pensioners; upon verification of the information on the registration form, the bank must issue an ID card for a fee not greater than $5.00.

RHODE ISLAND:

- The statute requires all depository institutions to cash federal, state and local checks up to $750 if the person presents either a Rhode Island ID card issued by the Department of Transportation or a picture ID issued by the Department of Elderly Affairs.
- The institution may refuse to cash the check if there is reason to doubt the validity of the ID.
- Depository institutions have voluntarily agreed not to charge a fee for cashing government checks.

Senator DIXON. Thank you, Mr. Stevens. That was very helpful.

Mr. Loundy, we're glad to have you here and appreciate your representation of the Independent Bankers Association of America. We're anxious to have your point of view.

STATEMENT OF RICHARD A. LOUNDY, CHAIRMAN OF THE BOARD, DEVON BANK, CHICAGO, IL, REPRESENTING THE INDEPENDENT BANKERS ASSOCIATION OF AMERICA

Mr. LOUNDY. Thank you, sir.

I appreciate the opportunity to present the serious concerns community bankers have about the proposals for government check cashing, lifeline checking and public disclosure of CRA ratings.

First, I want to emphasize that we strongly support the public policy goals behind these three issues. As community banks, we wholeheartedly provide these important services to our customers and our communities. While we support these important public policy goals, we strongly oppose the approach taken by Senator Metzenbaum's bills.

Those bills seem to be based on a premise that banks are all the same and are all essentially public utilities, which can provide congressionally mandated services at set prices. Unfortunately, this premise does not differentiate between those banks which are creating a problem and the thousands of community banks which are not.

The IBAA is opposed to a mandated government check cashing system for noncustomers. We are not convinced that there is a problem with cashing government checks of sufficient magnitude and scope to justify a federally mandated program. If the policy goal of Congress is to address the banking needs of those persons who do not presently have a bank account, mandating a check cashing service does not solve this problem.

One way to accomplish the goal is to link the cashing of government checks with some type of bank account. An account relationship, even a basic, no-frills account, provides the bank and the consumer with the opportunity to develop a banking relationship that provides a range of other options and products to the consumer while not leaving the banks defenseless to loss.

Banks have a very legitimate concern about cashing a government check for a noncustomer—the increased risk of fraud. Financial institutions face significant exposure by cashing government checks. If the check is counterfeit, altered or endorsed by someone other than the payee, the government will not reimburse the bank for the amount it paid to the individual.

Banks also face the serious problem of the slow return process for government checks. We may not learn that a check was fraudulent until several months after we accept it.

Officials at the Treasury Department recently indicated that there are more than 1 million claims filed each year for lost or stolen Treasury checks. Mr. Douglas just raised that figure to 1.5 to 1.8 million in a year. If you consider the many millions of checks issued by state and local governments and agencies across the nation, the potential exposure of banks on bad checks is extreme.

Senator Bond, in Chicago, there have been experiences where people have knocked off full sacks of checks by knocking off the storage boxes outside the post offices and waiting for the carriers on their routes.

The fraud problem can be best addressed by requiring that consumers receive their government payments by direct deposit into an account at a bank. Direct deposit is a reasonable compromise between the concerns of the banking industry and those of the consumer. It is a safe and reliable way to deliver funds to the consumer while greatly reducing the risk of fraud to the bank.

Direct deposit also provides benefits to the governmental agency issuing the funds since it is less expensive and more efficient than issuing paper checks.

There's clearly a need for better regulation of the non-depository check-cashing operations which we're calling here currency exchanges. These centers are concentrated in urban areas and the level of regulation varies greatly from State to State. Much of the public outcry about the difficulty in cashing government checks is the result of horror stories about check cashing centers charging exorbitant fees.

If the Congress is to take a comprehensive view of the check-cashing process, these check-cashing centers must be included in that effort.

Checking accounts provide safety and convenience for consumers and make it possible for them to be more active participants in our Nation's economy. Community bankers believe that basic banking services should be available for all consumers who desire them at a reasonable cost. However, the IBAA is opposed to the Government mandating all banks to offer a federally designed bank account. Many banks already offer their own version of a basic banking account on a voluntary basis designed by the bank to meet the needs and demands of its local customers. A mandated lifeline account would greatly restrict our ability to design accounts to meet the specific needs of our customers. It would write account terms and conditions into Federal law with the fees and charges set by the Federal Reserve Board. It would thus be necessary for our bank and most others now offering basic accounts to redesign those accounts to meet the specific requirements of the legislation and in the process reduce the number of options for consumers.

Our bank has a lifestyle checking account which almost qualifies under the requirements of Senate Bill 907. We charge 25 cents a check and $5 a month. Other banks in our area are even more generous. The Federal Reserve Board's Functional Cost Analysis, which is a study that the Federal Reserve does, in this case for Illinois for 1987, says that our costs are not 25 cents a check, they are 33¼ cents a check. And the monthly cost to maintain an account is $5.07.

Senator Dixon. What is that book in your hand, Mr. Loundy?

Mr. Loundy. This is the Functional Cost Analysis based on data furnished by the participating banks in the 7th Federal Reserve District for the State of Illinois for 1987. The Federal Reserve Board does a functional cost analysis each year of all the Federal Reserve Districts by state and nationally.

Senator Dixon. May we have that?

Mr. **Loundy**. Certainly.

Senator **Dixon**. I imagine that's very readily available.

Mr. **Loundy**. The 1988 ones are just coming out now. Ours had not arrived. We had ordered it but it hadn't gotten to us yet. They've been doing this for several years now. This provides functional cost information and has no provision in it for profit.

We believe that it is best to leave this subject to the competitive marketplace and not to public utility type legislation.

We are strongly opposed to the public disclosure by the agencies of a bank's CRA rating and evaluation. Disclosure of the CRA rating would have little meaning for the general public. In fact, the CRA rating could be confused with the CAMEL rating for safety and soundness exams and raise unnecessary concerns about the bank's overall health. The handling of this information by an uninformed media could produce tragic results, and I have dramatic personal experience to support that last statement.

If the Congress considers changes in the CRA we would strongly recommend that you extend that act to the nonbank banks, securities firms such as Merrill Lynch, insurance companies and other businesses which provide financial services. These other companies take deposits, often taking the funds out of the communities. They may provide some local credit, but they completely escape CRA requirements.

In conclusion, Mr. Chairman, we are very concerned about the regulatory burden these new consumer provisions would impose on community banks.

In the last 2 years the Congress has mandated extensive changes in four major areas—funds availability, credit card disclosures, home equity loans and adjustable rate mortgages. In addition to the hundreds of new pages of regulation to comply with, banks face the certain prospect of a sweeping increase in the enforcement powers of bank regulators under the FSLIC bill. The regulatory burden, particularly for small banks, is becoming overwhelming.

Thank you very much, sir.

[The complete prepared statement of Richard A. Loundy follows:]

TESTIMONY OF

RICHARD A. LOUNDY
CHAIRMAN OF THE BOARD

OF

DEVON BANK
CHICAGO, ILLINOIS

ON BEHALF

OF THE

INDEPENDENT BANKERS ASSOCIATION OF AMERICA

ON

GOVERNMENT CHECK CASHING, LIFELINE CHECKING
AND THE COMMUNITY REINVESTMENT ACT

BEFORE THE

CONSUMER AND REGULATORY AFFAIRS SUBCOMMITTEE
OF THE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

TUESDAY, JUNE 6, 1989

WASHINGTON D.C.

Mr. Chairman and members of the Subcommittee, my name is Richard Loundy. I am Chairman of the Board of Devon Bank in Chicago and I am appearing this morning on behalf of the Independent Bankers Association of America (IBAA). The IBAA is the only national trade association that exclusively represents the interests of our nation's community banks.

I appreciate the opportunity to present the serious concerns community bankers have about the proposals for government check cashing, "lifeline" checking and public disclosure of CRA ratings. I will address the questions you raised in your letter of invitation as well as provide some specific comments on the three bills introduced by Senator Metzenbaum in these areas.

First, I want to emphasize that we strongly support the public policy goals behind these three issues. As community banks, we provide important services to our customers and our communities. Indeed, our success is directly dependent on the health and well-being of our home towns and neighborhoods, so we strongly support the goal of providing access to basic financial services to all of our citizens. The CRA is based on the premise that banks have an affirmative obligation to help meet the credit needs of their communities. By their very nature, community banks support this premise and have been meeting the credit needs of their communities for years, long before the enactment of the CRA.

While we support these important public policy goals, we strongly oppose the approach taken by Senator Metzenbaum's bills. Those bills seem to be based on the premise that banks are all the same and are essentially public utilities, which should provide Congressionally-mandated services at set prices. Unfortunately, this premise does not differentiate between large banks and thousands of community banks.

We, like Congress, recognize that large financial institutions will not be allowed to fail. But community banks are different; we operate outside of the "public utility" support system. We operate under the discipline of the free market system and are allowed to fail. Community banks face a very different competitive and regulatory environment than large banks. We ask you to keep these differences in mind as you consider these issues.

GOVERNMENT CHECK CASHING

The IBAA is opposed to a mandated government check cashing system for noncustomers. We are not convinced that there is a "problem" with cashing government checks of sufficient size and scope to justify a federally mandated program. Last year's GAO report on this issue found that as of mid-1985, about 86% of all banks cashed U.S. Treasury checks for noncustomers. Of that number, more than half cashed Treasury checks free of charge. For those banks that charged for cashing a Treasury check, the median fee was about $2.

If the policy goal of Congress is to address the banking needs of those persons who do not presently have a bank account, mandating a check cashing service does not solve this problem. Those individuals would remain outside the mainstream of banking services. We believe that Congress should be looking for ways to bring this "unbanked" population voluntarily into the banking system.

One way to accomplish that goal is to link the cashing of government checks with some type of bank account. An account relationship, even a basic "no frills" account, provides the bank and the consumer with the opportunity to develop a banking relationship and provides a range of other options and products for the consumer.

Banks have a very legitimate concern about cashing a government check for a noncustomer -- the increased risk of fraud. Financial institutions face significant exposure by cashing government checks. If the check is counterfeit, altered or endorsed by someone other than the payee, the government will not reimburse the bank for the amount it paid to the individual. Banks also face the serious problem of the slow return process for government checks. We may not learn that a check was fraudulent until several months after we accept it.

Officials at the Treasury Department have indicated that there are over one million claims filed each year for lost or stolen Treasury checks, valued at over $400 million. If you consider the millions of checks issued by state and local governments across the nation, the potential exposure of banks on bad checks is substantial.

The fraud problem could be best addressed by requiring that consumers receive their government payments by direct deposit into an account at a bank. Direct deposit is a reasonable compromise between the concerns of the banking industry and those of the consumer. It is a safe and reliable way to deliver funds to the consumer while greatly reducing the risk of fraud to the bank. Direct deposit also provides benefits to the governmental agency issuing the funds, since it is less expensive and more efficient than issuing paper checks.

Direct deposit and other forms of electronic transfer of government benefits are clearly the wave of the future. Our Association is part of a group working to develop a government-wide Electronic Benefit Services (EBS) program to deliver benefits via plastic access cards using modern electronic technology. The Financial Management Service of the Treasury Department is the lead agency for this project. Similar efforts are taking place at the state and local level across the country.

Rather than perpetuating a costly, inefficient system of cashing paper checks which contains such tremendous risks for the consumers, banks and government agencies, the Congress should be encouraging further development of electronic transfer programs.

Mr. Chairman, Senator Metzenbaum's bill on government check cashing, S.906, is an improvement over earlier proposals but it still has a number of serious deficiencies. First, it does not establish an account relationship between the bank and the consumer. In fact, the bill provides that the bank cannot require any account relationships with the bank.

The bill does not require direct deposit of government benefits into a bank account, thus overlooking a safe and cost-effective means to provide consumers with access to their funds.

S.906 would require banks to cash government checks in amounts of $1,500 or less. This amount is a significant exposure for a financial institution, particularly a small bank. The $1,500 figure is likely in excess of the average government benefit payment and should be reduced. The $1,500 level would also require banks to keep much more cash on hand to meet demands of check cashers, adding to the cost and risk to the bank.

The bill does not provide sufficient protection for banks from fraud losses. A bank could reject an applicant for check cashing service only if it determines that an "intentional material misrepresentation" has been made by the applicant. Under this vague standard, a bank could be precluded from denying a check cashing registration even if it knew that the applicant had engaged in prior financial fraud.

The bill provides that the Federal Reserve Board may suspend the cashing of classes of checks where banks are experiencing "an unacceptable level" of fraud losses on such checks. As a community banker, I reject the assumption that there is an acceptable level of fraud losses on government checks that banks must absorb. This power of the Fed would be invoked only in the most unusual circumstances and only after the banks may have already lost thousands of dollars.

As you recall, former Chairman Proxmire attempted to draft a compromise version of his Glass-Steagall bill at the very end of the 100th Congress. Included in that measure was a government check cashing title which excluded banks with assets of less than $25 million, with an annual adjustment for inflation. There are similar small bank exemptions in other areas of banking law and we would urge the Subcommittee to consider such an approach, although with a substantially higher exemption level.

There is clearly a need for better regulation of the nondepository check cashing operations. These centers are concentrated in urban areas and the level of regulation varies greatly from state to state. Much of the public outcry about the difficulty in cashing government checks is the result of horror stories about check cashing centers charging exorbitant fees. If the Congress is to take a comprehensive view of the check cashing process, these check cashing centers must be included in that effort.

BASIC BANKING ACCOUNTS

Checking accounts provide safety and convenience for consumers and make it possible for them to be more active participants in our nation's economy. Community bankers believe that basic banking services should be available for all consumers who desire them, at a reasonable cost. However, the IBAA is opposed to the government mandating all banks to offer a federally-designed bank account. Many banks already offer their own version of a basic banking account on a voluntary basis. The terms, conditions and costs, if any, of these accounts are determined by the bank to meet the needs and demands of its local customers.

For example, my bank has six different types of checking accounts. One is specifically designed for senior citizens. We also have a basic account which we call the "Lifestyle Checking Account," designed for those who do not want to maintain any minimum balance in their account. This account has unlimited check-writing privileges at 25 cents per check and a monthly maintenance fee of $5. Most of the other banks in the Chicago area also have a variety of accounts including some type of basic account, so consumers have many options.

A mandated lifeline account would greatly restrict our ability to design accounts to meet the specific needs of our customers. It would write account terms and conditions into federal law with the fees and charges set by the Federal Reserve Board. It would thus be necessary for our bank and most others now offering basic accounts to redesign those accounts to meet the specific requirements of the legislation and in the process, reduce the number of options for consumers.

We have several specific concerns about Senator Metzenbaum's bill on basic banking, S.907. First, it does not sufficiently protect banks against fraud. The bill gives banks the authority to close a basic banking account on only two conditions: three separate overdrafts during a six-month period or "a pattern of fraudulent activity" in the account.

Mr. Chairman, we strongly object to the government requiring banks to tolerate a pattern of fraud. This contradicts the basic tenets of safety and soundness. Any single instance of fraud should be sufficient reason to close an account. The bill provides insufficient options for the bank to address overdraft problems. The size of an overdraft is often as important as the number of overdrafts.

The circumstances under which a bank may refuse to offer a basic account are also insufficient. The bill provides that a bank may reject an applicant only if it determines that an "intentional material misrepresentation" has been made in the information provided by the applicant. As with the government check cashing bill, such a vague standard could preclude a bank from denying a basic account even if it knew that the applicant had engaged in prior financial fraud.

Second, the bill provides an account-size limitation of $1,000 or less, but there is no reference to the income of the depositor or whether he has accounts at other financial institutions. Thus, it could be possible for middle or upper income persons with accounts at other financial institutions to open a basic banking account to take advantage of the services required by the bill.

COMMUNITY REINVESTMENT ACT

Community banks support the premise of the CRA, that financial institutions have an affirmative obligation to help meet the credit needs of our communities, consistent with safety and soundness. The fortunes of our banks are directly tied to the fortunes of our communities.

However, we are very concerned about the efforts of some to greatly broaden the CRA process into a credit allocation scheme with onerous recordkeeping requirements. For that reason, we strongly opposed the CRA provisions of H.R.5094, the bill approved last fall by the House Banking Committee.

As you know, former Chairman Proxmire attempted to craft a compromise at the end of the 100th Congress on CRA and a number of other issues. Two of the stated goals of the CRA provision were to shift the major CRA focus from the application stage to the regular examination process and to provide for more community input during the review. Under current policies, regulatory agencies already conduct CRA reviews at both stages. The agencies also have established systems for making community contacts during the review process.

There is one part of the Proxmire compromise that we could not support. We are strongly opposed to the public disclosure by the agencies of a bank's CRA rating and evaluation. Disclosure of the CRA rating would have little meaning for the general public. In fact, the CRA rating could be confused with the "CAMEL" rating for safety and soundness exams and raise unnecessary concerns about the bank's overall health.

A numerical CRA rating is ultimately a subjective judgement of an examiner and the evaluations can vary from one examiner to another and from one agency to another. Thus, it is possible that one agency could give a bank a "satisfactory" rating while another agency would rate the same bank as marginal. Or, one examiner with an agency could evaluate an institution quite differently than a coworker.

Public disclosure could also inhibit the open and frank discussions that must take place between bank officials and the regulators and make the CRA review process more adversarial. As a result, the discovery and correction of problems could become more difficult.

We believe that the disclosure provisions currently in place are adequate and properly balance the interests of both financial institutions and community groups. The federal bank regulators release aggregate CRA performance ratings through the Examination Council. Also, all banks have a notice in their lobby informing the public of their right to inspect the bank's CRA file.

If the Congress considers changes in the CRA, we would strongly recommend that you extend that Act to the nonbank banks, securities firms, insurance companies and other businesses which provide financial services. These other companies take deposits, often taking the funds out of the communities. They may provide some local credit but they completely escape CRA requirements.

As you know, there are CRA success stories out there. Unfortunately, most of the media attention is focused on confrontations and problems, rather than those success stories. Attached to my testimony are two articles from the Independent Banker, our Association's monthly magazine, which describe how two Illinois community banks are meeting the credit needs of their home towns and neighborhoods.

CONCLUSION

Mr. Chairman, we are very concerned about the regulatory burden these new consumer provisions would impose on community banks. In the last two years, the Congress has mandated extensive changes in four major areas: funds availability, credit card disclosures, home equity loans and adjustable rate mortgages. In addition to the hundreds of new pages of regulations to comply with, banks face the certain prospect of a sweeping increase in the enforcement powers of bank regulators under the FSLIC bill. The regulatory burden, particularly for small banks, is becoming overwhelming.

We look forward to working with you to achieve the goal of access to financial services for all who desire it. Through programs such as direct deposit and electronic funds transfer, it is possible to achieve that goal without imposing costly, quasi-public-utility burdens on the banking industry.

SUMMARY OF TESTIMONY

I appreciate the opportunity to present the serious concerns community bankers have about the proposals for government check cashing, "lifeline" checking and public disclosure of CRA ratings.

First, I want to emphasize that we strongly support the public policy goals behind these three issues. As community banks, we provide important services to our customers and our communities. Indeed, our success is directly dependent on the health and well-being of our home towns and neighborhoods, so we strongly support the goal of providing access to basic financial services to all of our citizens. The CRA is based on the premise that banks have an affirmative obligation to help meet the credit needs of their communities. By their very nature, community banks support this premise and have been meeting the credit needs of their communities for years, long before the enactment of the CRA.

While we support these important public policy goals, we strongly oppose the approach taken by Senator Metzenbaum's bills. Those bills seem to be based on the premise that banks are all the same and are essentially public utilities, which should provide Congressionally-mandated services at set prices. Unfortunately, this premise does not differentiate between large banks and thousands of community banks.

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One way to accomplish that goal is to link the cashing of government checks with some type of bank account. An account relationship, even a basic "no frills" account, provides the bank and the consumer with the opportunity to develop a banking relationship and provides a range of other options and products for the consumer.

Banks have a very legitimate concern about cashing a government check for a noncustomer -- the increased risk of fraud. Financial institutions face significant exposure by cashing government checks. If the check is counterfeit, altered or endorsed by someone other than the payee, the government will not reimburse the bank for the amount it paid to the individual. Banks also face the serious problem of the slow return process for government checks. We may not learn that a check was fraudulent until several months after we accept it.

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Rather than perpetuating a costly, inefficient system of cashing paper checks which contains such tremendous risks for the consumers, banks and government agencies, the Congress should be encouraging further development of electronic transfer programs.

As you recall, former Chairman Proxmire attempted to draft a compromise version of his Glass-Steagall bill at the very end of the 100th Congress. Included in that measure was a government check cashing title which excluded banks with assets of less than $25 million, with an annual adjustment for inflation. There are similar small bank exemptions in other areas of banking law and we would urge the Subcommittee to consider such an approach, although with a substantially higher exemption level.

There is clearly a need for better regulation of the nondepository check cashing operations. These centers are concentrated in urban areas and the level of regulation varies greatly from state to state. Much of the public outcry about the difficulty in cashing government checks is the result of horror stories about check cashing centers charging exorbitant fees. If the Congress is to take a comprehensive view of the check cashing process, these check cashing centers must be included in that effort.

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A mandated lifeline account would greatly restrict our ability to design accounts to meet the specific needs of our customers. It would write account terms and conditions into federal law with the fees and charges set by the Federal Reserve Board. It would thus be necessary for our bank and most others now offering basic accounts to redesign those accounts to meet the specific requirements of the

legislation and in the process, reduce the number of options for consumers.

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However, we are very concerned about the efforts of some to greatly broaden the CRA process into a credit allocation scheme with onerous recordkeeping requirements. For that reason, we strongly opposed the CRA provisions of H.R.5094, the bill approved last fall by the House Banking Committee.

We are strongly opposed to the public disclosure by the agencies of a bank's CRA rating and evaluation. Disclosure of the CRA rating would have little meaning for the general public. In fact, the CRA rating could be confused with the "CAMEL" rating for safety and soundness exams and raise unnecessary concerns about the bank's overall health.

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Public disclosure could also inhibit the open and frank discussions that must take place between bank officials and the regulators and make the CRA review process more adversarial. As a result, the discovery and correction of problems could become more difficult.

If the Congress considers changes in the CRA, we would strongly recommend that you extend that Act to the nonbank banks, securities firms, insurance companies and other businesses which provide financial services. These other companies take deposits, often taking the funds out of the communities. They may provide some local credit but they completely escape CRA requirements.

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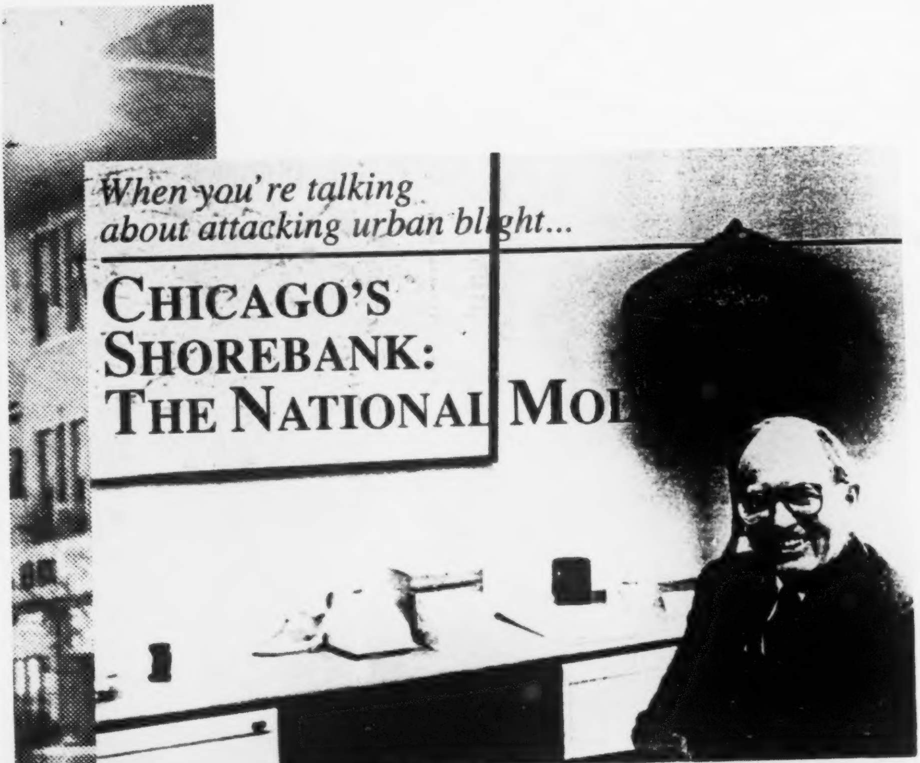


When you're talking about attacking urban blight...

CHICAGO'S SHOREBANK: THE NATIONAL MO

Shorebank Chairman Ronald Grzywinski: "We really believe that bank holding companies have enormous potential for community development."

by Brian Nixon
Associate Editor

Staff members of Chicago's Shorebank Corporation have a familiar passage to refer to should they ever need a reminder about their institution's mission. Ironically, the statement, which, incidentally, Chairman Ronald Grzywinski quotes almost from memory, is contained in Federal Reserve Board Interpretations of Regulation Y:

"Bank holding companies possess a unique combination of financial and managerial resources making them particularly suited for a meaningful and substantial role in remedying our social ills."

For the past 13 years Shorebank Corporation (a one-bank holding company for South Shore Bank) and its subsidiaries have been dedicated to improving the economic and social conditions of

Elspeth Revere, president of the Chicago-based Woodstock Institute: "We design programs that encourage banks to finance needed community development."

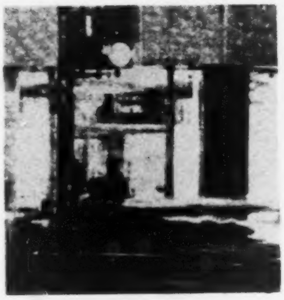
Mary Houghton, president of Shorebank and executive vice president of South Shore Bank: "To do this kind of work is not a quick fix."

Joan Shapiro is the bank's vice president of Development Deposits, an innovative program used to draw stable funds. Since 1974, South Shore Bank has attracted $48 million in Development Deposits, 39 percent of the bank's total deposits.

Photos courtesy of Shorebank Corporation

South Shore and its 80,000 residents. A long-range commitment to the neighborhood, located about eight miles south of the Loop, has helped stem the deterioration and inner-city blight that affected many of the nation's urban areas in the 1960s and 70s. Shorebank's successes have also provided important lessons for communities grappling with complex social and economic issues in the 1980s.

Perhaps most important of all, Shorebank has proven that a neighborhood's deteriorating conditions can be reversed.



As one staffer at the Federal Reserve Bank of Chicago puts it, Shorebank Corporation is the "national model" for community development. Few people will disagree. "We really believe that bank holding companies have enormous potential for community development," Grzywinski (pronounced Griz-WIN-ski) says. "As a society, we ought to create an environment for bank holding companies to foster community development."

CHAPTER TWO: ARKANSAS

A large map of Arkansas adorns the wall behind Ronald Grzywinski's dark red desk in his South Shore Bank office.

It represents the next chapter in the history of bank holding company community development corporation models, which Grzywinski is helping to write.

Similar to Shorebank Corporation's structure, community development efforts in Arkansas will be anchored by a holding company, Southern Development Bancorporation, and a bank. Unlike the Shorebank model, however, job creation and training will be Southern Development's primary focus.

It's a new test for community development corporations. "It'll be a great learning experience," Grzywinski, the chairman of Shorebank, says.

Spearheading the formation of Southern Development Bancorporation is the Winthrop Rockefeller Foundation, which has pledged $3.75 million to capitalize the venture. Plans call for the holding company to purchase a bank (between $60 million and $100 million in assets) sometime before winter.

An additional $4 million in capital is being sought from individual and institutional investors to further support the new venture. Along with Grzywinski, Mary Houghton, president of Shorebank and executive vice president of South Shore Bank, and Henry Morgan, a Shorebank director and former dean of Boston University's management school, will serve on Southern Development's board.

Along with the bank, four other Southern Development subsidiaries are planned. Southern Enterprise Group will be a non-profit corporation used to bring public and private resources together to operate economic development programs. A subsidiary of Southern Enterprise Group, Southern Ventures, Inc. will make equity investments of up to $300,000 in local firms. Opportunity Lands Corporation will handle real estate development projects. A seed capital company, the Good Faith Fund, will promote microenterprise development by making short-term loans to small businesses.

Initially, Southern Development Bancorporation will focus its development efforts in two economically depressed areas of Arkansas, each covering about two or three counties. Grzywinski, who spends about two days a week working on the Southern Development model, and other Shorebank consultants have visited Arkansas often while researching the project.

Those visits have featured stops in various communities around the state, including Dumas and McGehee in the Delta region. "In those towns we met with a lot of people," Grzywinski says.

Some of the strategies Southern Development plans to use to promote job creation are patterned after successful European programs. "In Europe, they're ahead of us in recognizing the critical job function that small business finance has in creating jobs," Grzywinski says. In the United States, "Nobody is really focusing on aggressively financing small business."

One strategy, for example, that the venture will borrow from Europe is the "small business incubator," where a warehouse or another under-utilized building is converted into affordable office space. Entrepreneurs rent individual offices, but share support equipment, such as copying machines and data processing systems. Small businesses are nurtured (through lower operating costs) until they can move out on their own, hence the concept's moniker.

Grzywinski expects the holding company to complete the purchase of a bank this year, marking the final stage before implementation of the program. "I think now that we have minimum capital commitments in hand, it'll move pretty quickly," he says. ■

A Bank's Rebirth

"Don't go to strangers" is an advertising slogan South Shore Bank uses to attract customers and remind them of its continuing commitment to the community. But in the early 1970s, the bank was, in many ways, a stranger in its own community. Economic conditions had changed, the flight to the suburbs was almost completed, and South Shore was quickly becoming an urban wasteland.

At that point, a series of important events happened.

South Shore Bank's pre-1973 management decided to move the bank downtown to the Standard Oil Building, after experiencing a prolonged decline in deposits. Before Shorebank Corporation (then known as the Illinois Neighborhood Development Corporation) purchased the bank, deposits were roughly halved to $42 million from a peak of $80 million. "It was absolutely clear that (the community) was going down the tubes," says Mary Houghton, executive vice president of South Shore Bank and president of Shorebank.

Meanwhile, Houghton, Grzywinski, and the rest of the current management team, Milton Davis, chairman of South Shore Bank, and Jim Fletcher, president of the bank, were working together at a bank in nearby Hyde Park—completing the formation of a minority lending department. "We were very successful," Houghton says. In minority lending, "We felt that we were outperforming the biggest banks in Chicago."

In 1971, after their success in Hyde Park, the four began working on a theory involving the use of a commercial bank as a vehicle for redevelopment. Grzywinski, in fact, spent two years at the University of Chicago's Adlai Stevenson Institute developing the appropriate business model that would test their theory. They believed the best tool for the job of community development would have to meet several requirements.

The right institution would feature: local authority and legitimacy; the ability to initiate actions; adequate resources; a defined geographic focus; a risk/reward system; a good leverage of risk capital; simultaneous economic and social development; and the ability to release local energies.

Grzywinski, Houghton, Fletcher and Davis ("I fondly refer to them as the 'gang of four,' " says Joan Shapiro, vice president of South Shore Bank) believed those needs were best met by a bank holding company structure with nonbank affiliates. "The core institution of the model is the commercial bank," Houghton says. She views South Shore Bank as the lead engine for development in the community.

As the four bankers refined their community development model, South Shore Bank and its former owners were preparing to pull up stakes and move to the Loop. "They saw their deposits declining," Houghton says. But the bank's managers failed to notice one important item: The community still wanted, and needed, the bank's services.

"The community fought the move and forced public hearings by the Office of the Comptroller of the Currency," Houghton recalls. In an unprecedented decision, the comptroller denied the bank's petition to move downtown. That was in 1972. By August, 1973, the "gang of four" had put together a consortium of institutional and individual investors to form a holding company community development corporation and had purchased South Shore Bank.

A Commitment to the Community

One of the first tasks handled by the bank's new management team included sprucing up its headquarters, located at the corner of 71st and Jeffery. A fresh coat of paint, new carpeting, and, later, a landscaped parking lot and remodeled lobby, sent a signal to South Shore's residents: The bank was committed to reversing the community's economic fortunes.

Some of the problems facing the community included deteriorating multi-family housing, commercial strips and single-family housing units. There are 34,000 housing units in the neighborhood; 28,000 are multi-family walk-ups. The community's demographics had also changed from the 1940s and 50s when South Shore was primarily a middle- and upper-income, white, professional neighborhood. About 95 percent of the community's residents are now black; a variety of racial backgrounds make up the other 5 percent.

South Shore was once a vibrant, attractive community. "This was an elegant neighborhood in the '40s and '50s," Houghton says. But could it begin making a comeback in the 1970s?

As Houghton recalls, "We had taken on an enormously difficult task. Nowhere in this city had that type of neighborhood deterioration been stopped."

Many of the neighborhood's classic, multi-family red brick dwellings were becoming dilapidated and single-family homes were in disrepair—results of prolonged urban disinvestment. The problem? People were afraid to in-

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vest money in their own community; market forces were working against South Shore by discouraging real estate investment.

Of Wrought Iron and Rehabs

Grzywinski compares communities to living cells. Communities, like cells, are constantly building up and tearing down. "In an inner-city neighborhood the tearing down process outpaces the building up," he says. In South Shore, the key to developing the community would be to reverse the process by promoting more building up.

People in the neighborhood had to be convinced that real estate investment in South Shore was a sound option. "To do this kind of work is not a quick fix," Houghton says. Members of the community needed to be shown that South Shore's red brick buildings "were once beautiful and they can be brought back to being beautiful again."

South Shore Bank also had to overcome the image projected by its previous owners that the bank was unwilling to lend money in the community. In late 1973, the

CDCs: OPENING NEW DEVELOPMENT AVENUES

The beauty of a community development corporation (CDC) is the versatility it offers banks in serving low- and moderate-income members of their communities. CDCs provide an avenue for development activities which banks cannot legally initiate.

They serve a wide variety of purposes. In rural areas, for example, CDCs have played an important role in providing housing for the elderly.

There are three ways a bank and a CDC can work together: a bank can form a CDC; buy an existing CDC; or join one in a cooperative venture. A CDC can be established as a subsidiary of either a bank holding company, a national bank, or a state-chartered bank.

The three organizational structures are similar.

A national bank may invest in a CDC if the following conditions are met: the project is of a predominantly civic, community or public nature and not merely private; the bank's investment in any one project does not exceed 2 percent of its capital and surplus; its aggregate investment of all such projects does not exceed 5 percent of its capital and surplus; and such investments are accounted for on the bank's books as "other assets."

The Federal Reserve requires no specific level of investment in a CDC by a bank holding company; the Board expects the holding company to fund prudently the CDC in accordance with safety and soundness considerations. State banking departments' guidelines concerning CDCs may vary.

The main consideration in determining a CDC's structure is the format which best complements the bank or holding company's present operations.

In some cases the best route is for a bank or bank holding company to purchase an existing CDC, or participate in a cooperative venture. That way the CDC's staff expertise is retained for the benefit of the community. "In a sense we're kind of encouraging that," says Jim Lowell, program manager, community affairs for the Federal Reserve Board. "They're almost transplanted investment bankers."

Federal banking regulators are actively promoting CDCs and are becoming increasingly aware of banks' Community Reinvestment Act (CRA) compliance. "Right now, CRA seems to be a hot issue," says Elspeth Revere, president of the Woodstock Institute, a Chicago-based community development consulting firm.

Both the OCC and the Federal Reserve host seminars on community development. "We want to provide new tools to banks with community development corporations, or banks interested in investing in such corporations, aimed at housing development and rehabilitation," Comptroller Robert Clarke, addressing an affordable housing roundtable hosted by the OCC in Washington last December, said.

Part of the regulators' interest in community development and CRA can be attributed to the work of organizations like Woodstock. The 13-year-old, non-profit firm advises financial institutions and community groups on development activities. "We design programs that encourage banks to finance needed community development," Revere says.

Activities of the Institute focus on three areas: applied research; policy development; and technical assistance. It has produced two in-depth studies of lending patterns in Washington, D.C., and Chicago, and is working on a similar survey in Denver, Colorado.

The Washington and Chicago studies were used by community groups in successfully negotiating with banks in the two cities for greater community investment. Both surveys concluded that a disproportionate amount of loans were being made in the suburbs.

Revere believes banks should redouble their development lending efforts. "The markets are created. How many people drank Bartles & Jaymes wine coolers before that market was created? Why not go out and look for the potentially good borrowers that are going to make the community better?" ■

new South Shore Bank was ready to begin work in its community, taking what Shapiro terms "a business approach to redeveloping neighborhoods."

The bank started small, offering mostly single-family mortgages from 1973 to 1976. "With very little energy," Houghton says, describing early development efforts, the bank attracted good-quality mortgage applicants. From that experience South Shore Bank began offering loans to rehabilitate multi-family housing units. "We started approving six-flat apartment building loans if they were owner occupied."

Much of South Shore's success (it has a 98 percent repayment rate on development loans) can be attributed to the conditions placed on some loans. Owner occupancy of a multi-family dwelling is important. Other guidelines include making external repairs to a housing structure. External appearances are important in community development, since it creates "momentum"—prompting other property owners to upgrade their housing units. "It has a positive real and psychological effect," Houghton says.

In South Shore, for example, ornamental wrought iron gates are gracing the front sidewalks of many multi-family, red brick units.

Probably the best testament to South Shore Bank's, and Shorebank Corporation's other real estate subsidiaries', success is the local market. Real estate is once again a "safe" investment in the community, and the market is growing. "In a way that no one could predict, a market grew in this neighborhood," Houghton says.

Much of the growth in the real estate market has been sparked by local entrepreneurs willing to invest both money and time. These investors borrow funds from South Shore Bank to rehabilitate multi-family units. To earn an adequate return entrepreneurs take a hands-on approach to rehabilitating South Shore's dwellings. "They essentially invest their own labor over a long period of time," Houghton says. "You've got to be able to run your own rehab jobs. They run their own crews."

Photo courtesy of Shorebank Corporation

South Shore's real estate renaissance is the key to future economic growth. "The fact that we appear to have stimulated the market is very important," Houghton says. "People don't imagine that a community like this would have a pool of talented real estate operators." The talent pool is growing, too. The community's leaders in housing rehabilitation help conduct classes on the functional parts of a building to acquaint budding real estate entrepreneurs with the rehab process. "A lot of information is traded from the professionals to the new guys."

While South Shore Bank has played a key role in community redevelopment, Shorebank's other subsidiaries also serve important purposes. The subsidiaries, created in 1977 and 1978, shoulder and initiate development activities which the bank cannot legally undertake.

City Lands Corporation, for example, is a for-profit real estate company whose charter permits residential and commercial development for the benefit of low- and moderate-income residents. Most of its efforts are concentrated on renovating large-scale, multi-family building projects. City Lands' developments stabilize and anchor targeted portions of the neighborhood so other local improvements can be made using public and private funding.

The Neighborhood Institute (TNI) assists low- and moderate-income people through job training and placement and by providing affordable housing. TNI's Housing Center has managed the rehabilitation of housing units in South Shore for cooperative ownership by moderate-income residents. TNI, a non-profit affiliate, is wholly supported by public and private grants and contracts. (It is Shorebank's understanding that when TNI was authorized in 1977, it was the first not-for-profit affiliate of a bank holding company in the country.)

A fourth subsidiary, The Neighborhood Fund, is a Minority Enterprise Small Business Investment Corporation. It finances growing, minority-owned companies that bring jobs and economic vitality to the community.

The three subsidiaries, plus South Shore Bank, are linked by their common goal—revitalizing South Shore. "They do different functions, but together the effect is going in one direction," Houghton says.

A Social Investment

South Shore Bank relies on an innovative program to attract stable funds. The program, Development Deposits,℠ appeals to social investors—individuals and institutions who seek a "social dividend" on their investment as well as a competitive rate of return.

The balance, or trade-off, between return on investment and social dividends "is really the essence of social investing," says Shapiro, the bank's vice president of Development Deposits. She is also the president of the Boston-based national trade association, the Social Investment Forum, which focuses on this issue. Since 1974, South Shore Bank has attracted $48 million in Development Deposits, representing 39 percent of the bank's total deposits.

Development Deposits are the bank's main community development tool. Each Development Deposit contributes to the pool of funds from which Development Loans are made. This helps explain the popularity of Development Deposits as a social investment, since investors know that their deposits are directly financing an innovative economic development effort.

A special Development Deposits program (and its only below-market-rate product) is the Investment Fund for Housing, a program which offers Rehab CDs—six-month or longer, $10,000 certificates of deposit. Interest on a Rehab CD begins at 1 percent below comparable market-rate CDs at the bank; the investor sets the rate and the term. The bank passes the differential between that and the market rate on to local borrowers in the form of a non-interest bearing, single-payment loan due only upon sale as an incentive to rehabilitate deteriorated housing units.

The success of these programs reflects the social responsibility philosophies of the bank's officers, directors, and investors. "There are much easier ways of making money than developing disinvested neighborhoods," Shapiro says. "But in the long run, do we have a choice?"

A Look at the Record

In 1986, South Shore Bank loaned $10.5 million in new development loans, and of that total $7.3 million went into multi-family mortgages. Since 1973, more than 6,000 multi-family housing units (18 percent of the neighborhood's total) have been rehabilitated through the developmental activities of the bank and Shorebank's other subsidiaries. South Shore Bank's net income was $1.47 million in 1986, a 16 percent increase over 1985.

Assets at year-end were $132 million. Return on assets has been more than 1 percent for the past three years. "Over the last couple of years, we've become quite profitable," Grzywinski says.

South Shore Bank's small business loan strategy is probably the only piece of the development puzzle that has not yet fallen into place. Although it has successfully used Small Business Administration loan guarantees (it's one of three SBA Preferred Lenders in Illinois and the only one in Chicago), the bank has had a difficult time reshaping the commercial strips that bisect the community. Part of the problem has been in encouraging small businessmen to upgrade their properties. "We just couldn't get adequate momentum going," Houghton says.

But Shorebank is using a new tack to promote small business development by shifting its focus to shopping center development. For example, City Lands plans to open up 40,000 square feet of space for small business investors in a new, 110,000-square-foot shopping center located on the corner opposite the bank at 71st and Jeffery. The shopping center is expected to be finished in less than two years. "The financing is in place, and the property has been assembled," Houghton says.

Two similar projects being considered along the 71st street commercial strip include a shopping center near Lake Michigan and the creation of a permanent farmers' market.

Less capital-intensive, non-retail forms of self-employment (service businesses, for example) are also being fostered. Those types of ventures are nurtured through "small business incubators" where underutilized building space is leased to several different enterprises. The small businesses share common office equipment, a copier, for example, which helps keep expenses down. "It's been a very successful program in England," Houghton says.

Shorebank plans to convert a warehouse now being used as its training center into a model small business incubator this fall.

By experimenting with small business incentives, Shorebank hopes to gain the same level of expertise that it acquired while reviving the community's real estate market. "We know that business," Houghton says. "But we knew we had to develop something new. We're now in a research and development phase."

A New Challenge

Austin, a community located six miles west of the Loop, represents the next step for Shorebank's community development team. It's larger than South Shore, in both geographical size and population (138,000). Similar to South Shore in the late '60s and early '70s, it is a community in a tailspin. Again,

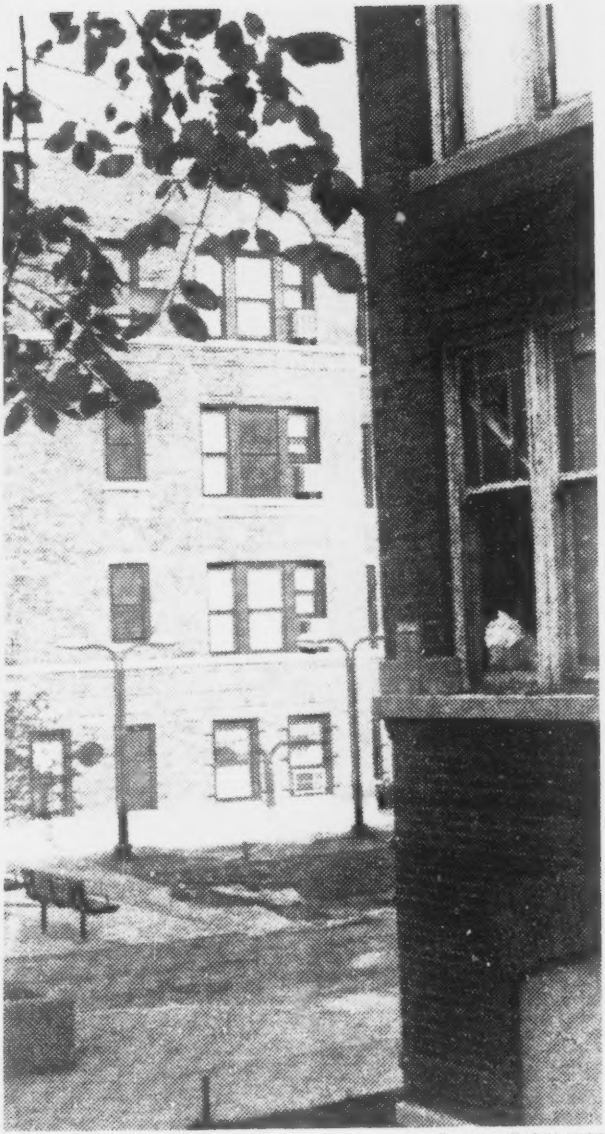

Photo courtesy of Shorebank Corporation

real estate lending is the key to reversing the neighborhood's fortunes.

"It's our largest community area," says Elspeth Revere, president of the Woodstock Institute, a non-profit consulting firm specializing in community development activities for low- and moderate-income urban and rural areas. "It's a neighborhood with a lot of problems, but it has some opportunities. The community has a number of experienced housing and economic development organizations that can work with the bank in addressing those problems."

According to the 1980 Census figures, 73 percent of Austin's residents are black, and 6 percent are Hispanic. The median income level in the community is $16,566, less than the city-wide median of $18,776. South Shore's median income level is $15,969.

City Lands Corporation, Shorebank's for-profit real estate subsidiary, is working on two large, visible, housing rehabilitation projects in Austin. The projects are meant to encourage owners of multi-family housing units to renovate their buildings.

To further promote rehabilitation efforts, South Shore Bank recently opened a loan production office in the community. Instead of opting for a full-service branch, the bank will concentrate its efforts in the development lending area. "We have a great deal of internal discussion about whether this strategy will work," Houghton says.

Shorebank's development team may be facing a tougher task in Austin than it confronted in South Shore. There's usually a slack period between the time a community development group enters a neighborhood and when people begin coming in for mortgage loans. In Austin, some fast action is needed to halt further decline in the community. "Because the multi-family housing is in worse shape than in South Shore in the '70s, we hope to cut the lag time," Houghton says. "My guess is that people in Austin will wait until the bank is there for about a year." ■

A Town Bursting With Pride Pulls Together

LENDING A HAND FOR COMMUNITY DEVELOPMENT

by Brian Nixon
Washington, D.C.

Harry McFall recalls growing up in Elmwood, Illinois, and the special contribution a resident made to the community.

Harry McFall, left, a director of the Farmers State Bank, and Fred Paige, the bank's president, are both involved in community development.

There was a fellow who ran a general store in the small town, located about 25 miles west of Peoria. Whenever McFall or his friends found an American Indian arrowhead they would go to the general store. The owner of the store would give children a piece of candy for an arrowhead. A stone Indian hand ax was even more valuable. It was worth a whole bag of candy.

The store owner kept the arrowheads and artifacts for the people of Elmwood to examine and enjoy. It was his way of preserving the heritage of a community that prides itself on its pioneer spirit.

McFall, a member of the Farmers State Bank's board of directors, hasn't forgotten the civics lesson. Now, he and several Elmwood residents and businessmen are working together, pitching in to improve the community.

"The whole community pulls together," McFall says, describing the pride that residents have in Elmwood.

A Common-Sense Approach

Elmwood's activities are not the stuff for a treatise on using federal grants to finance economic development. Business and community leaders have taken a commonsense, simple approach: Instead of leveraging large amounts of financial capital, they have concentrated on releasing the dynamics of human capital. That means getting people involved and tapping their areas of expertise for the benefit of the entire community.

"There's a lot of pride in the community," says Bob Lott, chairman of the $19 million-asset Farmers State Bank. The spirit is readily apparent.

While touring Elmwood's downtown area, Lott points to the new trees that have been planted along the sidewalk on a two-block section of Main Street. During the holiday season the trees, which were planted by the Elmwood Women's Club, will be decorated with lights. However, a weatherproof electrical outlet still needs to be designed.

After continuing the tour, the owner of a small manufacturing firm approaches Lott on the sidewalk, proudly displaying the prototype electrical outlet.

The town, which has a population of 2,300, has a strong school system that continues to build on the community's tradition of civic pride. "The school system has

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been rated one of the top ones in the state," Lott says. The students' average score on the ACT test is among the highest in Illinois.

On Sunday nights during the summer, one of the oldest city bands in the country (formed before the Civil War) plays in the gazebo in Elmwood's central park, across the street from the bank. The community's modern public library is privately endowed through the estate of a farm located just outside of town. There has been talk of using part of the farm as a museum, or even converting a large barn into a theatre.

FARMERS STATE BANK

Farmers State Bank of Elmwood faces central park, where the town's band performs on summer Sunday evenings.

A Victorian Downtown

The primary focus of development is Elmwood's downtown—restoring the buildings to reflect their Victorian heritage and encouraging new businesses to locate there. "We're trying to recreate a shopping center," says Fred Paige, the president of Farmers State Bank. "Most of our buildings have Victorian character and we're going back to that."

As part of the overall plan, an architect was commissioned to design a streetscape of the community's downtown shopping and business district. The architect's design calls for new paint on the buildings, attractive signs and colorful awnings.

Elmwood's businesses are not obligated to make the architect's recommended improvements. They are strictly optional. However, Lott, McFall and Paige, hope that as one or two downtown businesses improve their facades, the idea will spread. "The more people that you can have involved, the better the redevelopment will be," Paige says. "It is something that for a bank or a community takes a long-term commitment. It's not a quick fix."

To further encourage businesses to upgrade their buildings, Farmers State Bank offers a 2 percent interest rate reduction on business improvement loans.

Paige has taken an active role in courting new businesses for Elmwood. Currently he's working on getting a new hardware store for the downtown. A two-story building next door to Farmers Sate Bank, which the bank is restoring, may become home to a haberdashery. Another historic building, the Palace Theatre, has been refurbished, and a turn-of-the-century hotel has become a retirement center. "It has not been very difficult at all to sell the community," Paige says. "People are looking for quality of life."

Working for the Future

Lott and McFall are familiar with projects that take plenty of nurturing before they reach fruition. Both have worked to restore local

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farm land that had been strip mined and laid waste.

Another project the two have worked on since 1961 involves Interstate 74. State Route 78, which goes through Elmwood, meets the interstate about three miles north of town. When the interstate was built, there was no direct interchange for Elmwood. Lott and McFall have fought for an Elmwood interchange, even going as far as traveling to Washington in 1965 to lobby for it.

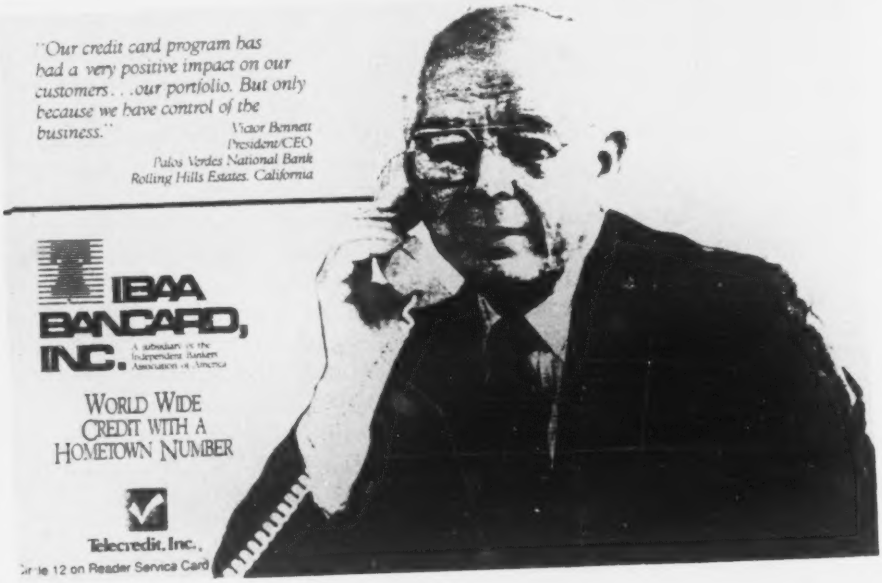
Although their efforts have been largely unsuccessful (Elmwood finally did get a sign placed at exit 71, closer to Peoria), Lott says he'll continue to press the interchange issue. "I'm not giving up on it yet," he says.

Tourism is one area for growth in the community. Elmwood was sculptor Lorado Taft's hometown. The home of a pioneer family is now the Lorado Taft Museum and the headquarters for the Elmwood Historical Society. Taft was commissioned to design the Midway at the Columbia Exposition in Chicago in 1893. It later became known as the Chicago Midway. One of Taft's sculptures, "The Pioneers," is displayed in Elmwood's central park. The sculpture, which depicts a young family of Illinois settlers, bears a dedication "To the pioneers who bridged the streams, subdued the soil, and founded a state."

"The Pioneers" is also a part of Farmers State Bank's logo, and its marketing strategy. "All of our advertising is done with that statue," Lott says. "We call ourselves the pioneer bank." It's an appropriate description. The bank was founded in 1864, 12 years after William J. Phelps laid out the community. The histories of the town and Farmers State Bank are closely linked. The same is true for what lies ahead. "The future of Elmwood is bright," Lott says. ■

New trees have been planted along Main Street by the Elmwood Women's Club.

Lorado Taft's sculpture, "The Pioneers," is displayed in Elmwood's central park.



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Senator DIXON. Thank you very much, Mr. Loundy.

Mr. John P. Kelly, Jr., President of the National Bankers Association, we welcome you, sir.

STATEMENT OF JOHN P. KELLY, JR., PRESIDENT, NATIONAL BANKERS ASSOCIATION

Mr. KELLY. Thank you. Good morning, Mr. Chairman, Senator Bond and Senator Metzenbaum.

My name is John P. Kelly, Jr. I'm the president of the National Bankers Association, which is the 62-year-old trade association for minority and women-owned banks.

Mr. Chairman, I would first like to thank you for giving me the opportunity to appear before the subcommittee today to express our membership's views on these important legislative issues of "lifeline" or basic banking services, government check cashing and the Community Reinvestment Act.

As stated in our written testimony, minority banks operate in the communities with the larger concentrations of low income Americans and our position on the issues of basic banking, government check cashing and CRA has been set forth in our written testimony.

Therefore, my oral testimony today will focus on addressing the questions raised in the chairman's May 23, 1989 letter and a summary of the position of the minority banks on some key provisions of S. 906 and S. 907.

On the first question of the primary check cashing problem, the primary problem with cashing government checks was none of the ones cited in the letter. The primary problems are twofold.

The first has to do with the ease with which a recipient can claim nonreceipt, loss, forgery or any other reason that would result in a reissuance of the check by the government, and a loss to the bank or entity that encashed the item. The recipient merely files an affidavit—and there appears to be no further investigation or accountability required. Even in instances where other evidence existed such as photographs or fingerprints, the simple filing of an affidavit is sufficient to result in a loss to a financial institution. This has obviously led to a greater amount of fraud loss on government checks than on other checks cashed in the banking system.

Coupled with this has been the time period during which the government has had to return checks cashed, for the reasons cited above. In the past this was 6 years. More recently this has been reduced to 18 months. The time period that the banking industry has to return a nongovernment check is 24 hours.

If it were not for these two factors, there would not be a problem in cashing government checks.

The second and third question, useful alternatives or supplements to S. 906 and the best ways to minimize fraud with government check cashing, the most useful alternatives or supplements to S. 906 and the best way to minimize fraud with government check cashing is to move in the direction of providing all government benefits electronically via point of sale and automated teller machines. The technology exists and the recipients and the government would both benefit from this type of delivery mechanism.

Any proposed legislation should encourage current Treasury efforts in this area. Our written testimony makes reference to the Treasury's efforts in the area of Electronic Benefits Services. Our national payments system is moving in this direction and away from paper based transaction, legislation that does not address this trend will be outdated the minute it is passed.

Should everyone have a checking account? Any one of a number of the surveys cited in our written testimony indicate that not everyone wants to have a checking account and their desires in that regard should be respected in a free society.

We would agree with the Federal Financial Institutions Examination Council that there are three fundamental needs that the financial system should meet. They are the need for a safe and accessible place to keep money, a way to obtain cash, and a way to make payments to third parties.

Our financial payments system should and does provide for these fundamental needs and the movement to an electronic delivery system would meet the needs of virtually all Americans, without the need to have a "checking account," particularly if they chose not to have one.

I'd like to merely summarize the position of minority banks on the key provisions of S. 906 and S. 907 as presented in our written testimony.

On the subject of "basic banking," 75 to 90 percent of the consumer accounts in most minority financial institutions have an account balance of less than $1,000. By definition per S. 907, minority financial institutions are already providing banking services to individuals with $1,000 or less in their account.

For minority banks to be denied their free market right to price these services based on each bank's operating cost would deny minority financial institutions the ability to insure profitable operations of over 75 percent of their deposit base. Since these accounts would represent a much smaller percentage of the deposit base of majority institutions, the burden placed on minority institutions by such legislation would be disproportionate and unduly and significantly interfere with their ability to operate successfully in a free and competitive market environment.

Such legislation would also penalize the very group of institutions that have been serving the type of customers this legislation is intended to help. Further, it would make it even more difficult to profitably operate a minority financial institution.

Requiring the cashing of government checks for nonbank customers, without significant changes in the investigation or accountability of claims and the time period that the government is allowed to return checks, would deliver another serious blow to the successful and continued operations of minority financial institutions.

On CRA, the CRA needs to be redesigned to be a more effective regulatory instrument. While the intent is there, it lacks the necessary inducements and assumes that all banks can be held to a standard set of criteria. Even if that were operative, as legislation, it lacks in the area of enforcement and uniform application. We believe that a redesign of the CRA program to include incentives would be more effective. The incentives could take many forms and be designed to have minimal budgetary impact. In this way banks would have an incentive to comply with CRA and those banks that already do so as a matter of policy or practice would be further encouraged to meet the financial needs of our low income communities.

In conclusion, I would encourage this subcommittee to closely examine the potential consequences of any legislative initiative in the areas of government check cashing and basic banking services on small and minority-owned banks and their communities and to evaluate the alternatives suggested before enacting legislation that may drastically reduce available banking services and perpetuate a system which is costly and inconvenient to recipients.

I thank you.

[The complete prepared statement of John P. Kelly, Jr. follows:]

Statement of John P. Kelly, Jr.
President
National Bankers Association
Before the Subcommittee on
Consumer and Regulatory Affairs
Committee on Banking, Housing and Urban Affairs
United States Senate

June 6, 1989

INTRODUCTION

Good Morning Mr. Chairman and members of the Subcommittee. I am John P. Kelly, Jr., President of the National Bankers Association, the 62 year old trade association for minority and women-owned banks.

Mr. Chairman, I would first like to thank you for giving me the opportunity to appear before the subcommittee today to express our membership's views on these important legislative issues of government check cashing, "lifeline" or Basic banking services and the Community Reinvestment Act (CRA).

BACKGROUND

As you all know, recent and significant changes in the structure, marketing practices and regulation of the financial services industry have led many depository institutions to assess and ultimately revise the price at which services are offered. They have also consolidated or eliminated unprofitable services to maintain their profit margins, manage risk, and reduce costs. The increases in service charges and minimum balance requirements for some deposit services, have priced these deposit services beyond the financial reach of some consumers. Moreover, the closing of less profitable facilities in low- to moderate-income areas has denied many neighborhoods and communities convenient access to basic banking services altogether.

These problems, which proponents of basic banking services would argue imposes hardships on those remaining and prevents others from even entering the system, is undeniable. One obvious manifestation has been increasing public debate over whether there should be an obligation for depository institutions, because of the nature of their federal charters and the resulting economic benefits, to provide basic banking services to all individuals who require it. There is no consensus as to what extent and to whom these services should be offered. The legislation that is the focus of our discussion today is one response to the problem, however, there is another side to this story and alternatives to this legislative approach we would like to offer for your consideration.

The total number of minority and women-owned financial institutions in this country account for less than one percent of the entire financial services industry and date back to 1888. These early institutions arose to meet the financial need among ethnic minorities in America that majority-owned financial institutions either would not or could not satisfy. Technological advances, demographic movements, and increasing competition notwithstanding, minority-owned and operated financial institutions have maintained their commitment to providing available and affordable financial services to their predominately minority, low-income, inner city communities which have been and continue to be abandoned by other institutions, many of whose activities created the impetus for these very debates. This brief background of the important mission of minority-owned financial institutions is not offered to suggest that other depository institutions are any less committed to their communities, but only to suggest the unique circumstances in which most minority-owned financial institutions operate.

BASIC BANKING SERVICES

S. 907 essentially requires all depository institutions to provide a basic financial services account for individuals who have $1,000 or less on deposit at that institution. This "basic" account would permit at least 10 withdrawals per month and be subject to "minimal" service charges to be established by the Federal Reserve Board. There are also prohibitions on prerequisites that "discriminate" against low income individuals or that require exclusive use of automated teller machines or other nonteller services.

While the presumed goal of providing low-income and elderly individuals with access to basic banking services represented in this bill are laudable to be sure, by virtue of the $1,000 deposit limitation for institutions providing the services, it is not narrowly tailored to truly low-income individuals. In addition, it results in unfair and disproportionate burdens on minority-owned financial institutions already operating in low-income areas, and it does not take into account the various factors other than pricing of deposit services which explain why some individuals do not hold deposit accounts.

According to an article appearing in a 1987 Federal Reserve Bulletin entitled, "Basic Banking", the Unidex Corporation conducted a survey which focused on the current financial behavior of consumers to better understand the reasons why certain families do not hold deposit accounts. The survey response indicated that nearly half the respondents either did not want an account or did not need an account. Among those who indicated that they did not want an account, the most cited reason was that they preferred to use cash or money orders or had difficulty keeping an account balance. Others indicated that no financial institution was conveniently located or they simply did not trust financial institutions. While some did indicate that they could not afford such an account, most indicated that they did not have enough money to make having an account worthwhile.

The same Federal Reserve Bulletin article cited a 1986 survey sponsored by the Federal Reserve Board which collected information about deposit account ownership from a nationally representative sample of families. The results of this survey were consistent with those found in the Unidex survey except that no respondents in the 1986 survey cited high service fees or minimum balance requirements as the main reason for not having an account. The majority of respondents without an account indicated they would not write enough checks or did not have enough money to make having an account worthwhile. A very small group indicated that they did not have an account because financial institutions were either inconveniently located or not open at convenient hours.

According to an American Bankers Association survey conducted in the last quarter of 1987, 52 percent of banks nationwide already offer basic accounts, up from 44 percent in 1986. Based on this trend and information gathered from these and other similar studies and surveys, merely reducing fees for deposit account services may be attractive only to the most price-sensitive families without accounts. Whether the great majority of families who cite inconvenient hours of operation, location, preference for other nondepository providers of financial services (such as check-cashing facilities and sellers of money orders) and minimal expenditures requiring transaction accounts would benefit from basic banking services is far from conclusive.

The type of community in which a financial institution operates will have a direct impact on demand for its basic banking services. Institutions such as minority-owned institutions in predominately lower-income neighborhoods would likely find the demand for their basic banking accounts far different from that found by upscale institutions operating in higher-income locations. If basic banking programs cannot be operated profitably, or at least on a break-even basis, minority-owned institutions and those located in lower-income areas that offer such accounts will operate at a competitive disadvantage. Because demand for these basic account services and government check cashing services will likely be strong in these low-income areas, the imposition of these extra costs may force more banks to close or relocate; potentially making financial services even less available in low- and moderate-income neighborhoods and thus defeating the purpose of the legislation.

The National Bankers Association conducted a recent survey to determine how a legislatively mandated basic bank account like S. 907 requires would affect its member banks. Respondents indicated not only that a majority currently offer some form of

basic banking service to truly low-income and elderly individuals, but also that 75 percent to 90 percent of their individual account holders have $1,000 or less on deposit. Many indicated further that the increased cost to their banks resulting from enactment of this bill alone could force them to close their doors without taking into account the affect of a government check cashing requirement.

The substantial disproportionate burden that S. 907 would impose on minority-owned banks is simply too onerous for this segment of the financial services industry to bear. This bill would also create an environment for bank failures in low-income minority neighborhoods which are already underserved by majority-owned financial institutions. Rather than addressing legitimate problems which minority-owned financial institutions were created to address, this bill could create an even larger problem placing additional pressure on the already strained resources of the financial services industry insurance fund.

GOVERNMENT CHECK CASHING

S. 906 provides that check cashing depository institutions must cash any check in the amount of $1,500 or less issued by the U.S. Government, any State, any unit of local government, or any agency thereof, for any customer if the check is made payable to the bearer and such customer is properly registered with the institution pursuant to Federal Reserve Board regulations.

While the intent of this legislation appears to address legitimate concerns regarding low-income and elderly individuals having difficulty cashing government issued checks, this bill as currently drafted is overly broad, and by reasons of unique circumstances in the marketplace, would have disproportionate impact on minority-owned financial institutions.

Minority-owned financial institutions operate by and large in low-income, high crime inner city neighborhoods. As a result, their exposure to large numbers of government issued check bearing customers would be multiplied by enactment of this mandatory check cashing requirement. NBA believes the scope of any legislative initiative attempting to provide such a service should be carefully tailored to those who are less likely to have a bank account but who actually need one, and certainly not to every recipient and every category of government check.

In our view, fraud and the difference between the time period that a government check (18 months) can be returned and any other check (24 hours) presents the biggest problem for our institutions when faced with cashing a government check for a non customer. To illustrate the excessive minority-owned bank exposure to fraud, Seaway National Bank President Walter Grady (Chicago, IL) indicated recently that prior to a check cashing policy change in 1980, between 70 percent and 80 percent of all fraudulently cashed checks at that institution were issued by some unit of government.

B. Doyle Mitchell, Chairman of the Industrial Bank of Washington (Washington, D.C.) indicated that prior to a check cashing policy change at his institution, his bank was exposed to a number of check fraud schemes one of which lasted for several years and resulted in his bank having to absorb all fraud losses which accrued during that period. The fraud involved an individual who had a joint account with a social security recipient who died. This individual continued to cash the social security checks for the deceased individual until the Social Security Administration detected the error several years later. While the extent of liability has now been reduced to 18 months, several instances of this type of error can create serious losses for a small institution.

In addition to fraud, there are other operational impacts and costs associated with mandatory check cashing which minority-owned institutions would have to disproportionately bear. For instance, the burden of employing and training additional tellers to accommodate, assuming such needs can be accommodated, the increased numbers of government issued check cashing customers would be borne more heavily by minority-owned institutions simply because they serve low-income neighborhoods. These same institutions, which often operate on very thin profit margins, can least afford to absorb the additional costs.

Moreover, the increased volume of every category of government check cashing non-customers could conceivably include numerous individuals such as construction workers engaged in government sponsored projects. Because government payments usually arrive on the same day for all recipients, overcrowding on payment days would severely strain the banks resources as well as inconvenience and alienate its regular customers creating the real potential for a reduction in core deposits. Handling larger amounts of cash during certain high level activity periods of government check cashing also increases the bank's costs to transfer and store the cash, and increases the bank's, and its customers, exposure to robbery.

Although Section 2(b)(4) of S. 906 permits the Federal Reserve Board to set permissible fees for check processing cost, it does not require the Board to set these fees at levels which assures that all banks will recover their costs. Different depository institutions, particularly small institutions which do not have the advantages of economies of scale, which larger banks enjoy, will encounter different levels of demand for check cashing services. A fee set by regulation is therefore not likely to be appropriate for all banks.

The section 2(c) exception which permits a depository institution to deny provision of a government check cashing service to any individual who has either a transaction account at another institution or a government check cashing relationship at another institution is essentially meaningless for small institutions who will often not have the resources to initially investigate and monitor these types of relationships nor investigate the accuracy of signed statements provided for in Section 2(d)(2) attesting to the situation providing the 2(c) exception.

While Section 2(d)(3) provides that an institution may reject registration of an applicant if intentional material misrepresentation has been made, smaller minority-owned institutions will often find this type of examination too costly and time consuming to conduct to adequately protect the bank from the numerous registration applications.

These are but a few examples which illustrate the significant risks and the substantial disproportionate burdens that mandatory check cashing legislation would impose on minority-owned financial institutions. Additionally, this approach promotes the paper check distribution of payments and thereby reduces the incentive to explore the development of less expensive, more efficient and convenient alternatives, which will be suggested in alternative approaches discussed later.

COMMUNITY REINVESTMENT ACT

In response to public policy issues and concerns raised by the antiredlining movement of the 1970s, Congress, on December 18, 1975, enacted the Home Mortgage Disclosure Act (HMDA), the first of two legislative initiatives designed to encourage financial institutions to help meet the housing credit needs of their communities. Next, enforcement powers were sought for regulatory agencies to encourage these institutions to better serve the needs of their entire communities and to assess the degree to which they were in compliance. Accomplishment of this goal was attempted in 1977 by enactment of the Community Reinvestment Act (CRA).

Now almost twelve years after enactment of CRA, questions regarding how best to encourage greater compliance efforts by lending institutions are posed in public debates such as this. This question is difficult to answer without first acknowledging the numerous enforcement problems encountered by regulatory agencies resulting from the lack of specific direction contained in, and the ambiguous nature of the Community Reinvestment Act itself. Secondly, greater compliance can only be determined after some attempt at assessing current compliance efforts, which in and of itself is a difficult task.

In 1985, the General Accounting Office (GAO) attempted to assess the impact of CRA on lending patterns in low- to moderate-income neighborhoods, but found major obstacles which made it impossible to conduct a reliable evaluation. One problem encountered by GAO was that measures now used to asses the extent of institutional compliance with CRA were not available prior to enactment of CRA. Other legislative initiatives including the Depository Institutions Deregulation and Monetary Control Act of 1980 and the Garn-St Germain Depository Institutions Act of 1982, also significantly affected investment behavior of financial institutions in the years since CRA.

These factors, and others including: (1) mortgage interest rate fluctuations, (2) increased volume of mortgages insured by the Federal Housing Administration, and (3) increased availability of mortgages originated by mortgage bankers not covered by CRA, make it impossible to establish the extent to which changes in lending patterns by location are a result of CRA, as distinct from being the result of other factors.

Some have suggested that disclosure of CRA ratings might be one solution to greater compliance. Such disclosure, in our view, would offer no articulable benefits when one considers that questions about whether bank examiners themselves understand currently required disclosed information are often raised still by legislators, academic researchers and many others who have examined implementation of CRA over the years. For example, in order to measure a community's credit needs and assess whether a local lending institution's efforts satisfy those needs, as required by CRA, some understanding of economic development -- a community's long term housing plan, local demographic changes, and a host of other urban development concepts is required. These concepts are not totally familiar to the traditional bank examiner, much less the average lay person.

Further, one of the main criticisms of CRA has been the arbitrary nature of the rating system used by bank examiners to assess an institution's performance in serving the credit needs of its community. Given the industry's critical role in the functioning of the monetary system in this country and its absolute dependency on public confidence, the potential for irreparable harm resulting from misconstrued rating information challenges the wisdom of making such information available to even the most sophisticated consumer.

At this point, it should be noted that not all depository institutions need stronger encouragement for greater compliance with CRA that new legislation may require. There are many examples from across the country which clearly show that many lenders, particularly minority-owned financial institutions, view reinvestment as not only good public policy, but an obligation. This is not to suggest that these lenders are altruistic, but instead that prudent lending is profitable no matter what part of the city, or nation, it is contemplated.

One prime example was illustrated in an Atlanta Journal article published in 1988, which alleged widespread discriminatory banking practices in Atlanta, Georgia. The writer measured lending to Black and/or low-income neighborhoods and found that the lender with the best record of inner city lending in Atlanta, also had the lowest loan loss rate. The fact that the lender, Citizens Trust Bank of Atlanta, happens to be a well established Black-owned bank and member of the NBA suggests the need for Congress and the regulators to consider encouraging partnerships between majority-owned and minority-owned financial institutions as a means of encouraging greater CRA compliance. Because most minority-owned banks are already located in low-income urban areas, providing an ideal vehicle through which the economic and business needs of these communities can be met, such partnerships would be a positive move in the direction of realizing the legislative intent of CRA, elimination of redlining and revitalization of inner city neighborhoods.

ALTERNATIVE APPROACHES

As with CRA, NBA believes in the "carrot" versus the "stick" approach for addressing the problems of government check cashing and provision of basic bank services. Providing incentives to depository institutions as encouragement for providing available and affordable financial services to their customers and meeting the credit needs of their communities, in our view, is much more effective. Legislation which mandates specific performance requirements which restricts natural market demand forces which operate to determine sufficiency of services provided also further inhibits innovation. As suggested above, rather than assisting the elderly and those living in low-income areas as the proposals currently being considered apparently intend, enactment of these proposals as drafted may instead frustrate efforts by institutions sensitive to the needs of their communities and even reduce the current availability of financial services.

ELECTRONIC BENEFIT SERVICES PROGRAM

One example of innovation that should be encouraged is a less expensive, more efficient and secure alternative currently being developed and promoted by the Department of the Treasury. This program, the Electronic Benefit Services (EBS) will provide a governmentwide service to deliver benefits via plastic access cards using modern electronic technology. Goals of the EBS program include:

(1) Enhancement of the level of services to the benefit recipients population who, for whatever reason do not hold deposit accounts, by offering an electronic delivery alternative;

(2) Reduction of the cost associated with delivering benefits through Automated Teller Machines (ATMs) and Point-of-Sale (POS) terminals over paper-based systems, and;

(3) Encouragement of the multiple delivery of benefits through a single plastic card to those recipients without deposit accounts receiving several different benefits.

Advantages of such a system include:

* Recipients would have immediate access to funds;

* Personal deposit of paper checks will be eliminated;

* Recipients, particularly handicapped and elderly individuals, would be protected from theft of the paper check itself and/or theft of cashed funds during traditionally high crime periods for larceny and assault;

* Recipients may draw funds as needed, and

* The direct deposit feature encourages recipients to maintain accounts and thereby encourages savings.

Treasury's Financial Management Service (FMS) is currently seeking input from all perspectives in the development of a blueprint for this governmentwide EBS program and plans to have a blueprint constructed by the end of FY 1989. I have been asked to be a part of the working group which is responsible for identifying and researching the issues surrounding the development of the EBS program and assisting in resolving related concerns.

My experience with a similar program during my term as President of Midwest National Bank in Indiana suggests that this approach is workable and a far more efficient and secure alternative to the government check cashing proposals under consideration by this Subcommittee.

CONCLUSION

In conclusion, I would like to strongly encourage this Subcommittee to closely examine the potential consequences of any legislative initiative in the areas of government check cashing and basic banking services on small and minority-owned banks and their communities and to evaluate the alternatives suggested before enacting legislation that may drastically reduce available banking services and perpetuate a system which is costly and inconvenient to recipients.

Thank you.

Senator DIXON. Thank you very much, Mr. Kelly, for the perspective that you place on this issue. It's a very interesting one. We will develop it in the question and answer period.

Mr. Robert J. Sell of the National Legislative Council, American Association of Retired Persons, from Chicago. We're delighted to have you here, Mr. Sell.

STATEMENT OF ROBERT J. SELL, MEMBER, NATIONAL LEGISLATIVE COUNCIL, AMERICAN ASSOCIATION OF RETIRED PERSONS

Mr. SELL. Thank you, Mr. Chairman.

Mr. Chairman, Senator Bond, Senator Metzenbaum, good morning.

The American Association of Retired Persons appreciate this opportunity to comment on S. 907, the "Basic Banking Services Access Act of 1989" and on S. 906, the "Government Check Cashing Act of 1989." We are pleased that the Senate Banking Committee is highlighting the issue of access to banking services through these hearings.

Assuring the safety and soundness of depositors' funds has, understandably, been of primary importance to the 101st Congress. However, once depository funding problems have been resolved, AARP believes the Congress should make certain that all potential banking customers have access to affordable banking services. This action is essential to fully restore public confidence in the ability of the financial services system to respond to their most basic depository needs.

Today, access to simple banking services is often difficult, sometimes virtually impossible. Financial institutions now charge for services they used to offer free and have increased fees on other services.

The new or increased fees, coupled with more onerous account terms and conditions, have placed banking services beyond the reach of some low and moderate income, and elderly people to the point where they simply do not have bank accounts. For those without an account, paying bills becomes difficult and personal safety is jeopardized.

Since many people need access to basic, no-frill bank accounts, AARP believes Congress should require financial institutions to provide individuals with access to a minimal level of banking services.

Passage of S. 907 will assure the ready availability of basic, no-frills banking accounts for many low and moderate income people. AARP hopes the Senate Banking Committee will support the basic banking bill, S. 907.

AARP is also concerned that many financial institutions have adopted "If you don't bank here you can't cash here" practices. Often these policies extend to government checks, State government checks and local government checks.

People without bank accounts obviously have the greatest difficulty cashing government checks. However, even people with accounts are encountering problems. Many financial institutions require their account holders to maintain a balance sufficient to cover the amount of the check being cashed. Thus, if you get a $500 monthly retirement check, some institutions may require you to have a $500 balance on deposit to cash your retirement check at your own bank.

Tragically, many of these are low income people who need their available funds to meet ordinary living expenses. They simply cannot afford to forego timely access to their money. Those who cannot get their government checks cashed at financial institutions are relegated to cashing their checks at expensive check cashing services.

To alleviate this problem, passage of S. 906 would require institutions to cash government checks. AARP therefore urges passage of S. 906.

Some comments concerning AARP's opposition to mandated direct deposit. AARP encourages its members to utilize direct deposit services. However, it must be recognized that different consumers have different needs. The individual must retain the prerogative of choosing the depository method that best suits his or her particular needs.

To establish mandated direct deposits as a prerequisite for access to banking services is, in AARP's view, both unacceptable and inappropriate. AARP opposes mandating direct deposit as a necessary precondition for the receipt of a basic banking account or the use of government check cashing privileges for the following reasons.

Many older Americans are reluctant to use direct deposits. In spite of aggressive efforts by the Treasury Department and by financial institutions to encourage direct deposits, only 47 percent of Social Security beneficiaries use direct deposit. Thus, over 20 million Social Security beneficiaries do not use direct deposit.

Acceptance of direct deposit is lowest among the low income population.

Consumers are experiencing difficulties in resolving direct deposit problems. In fact, some Social Security beneficiaries have had to forego access to their funds for as long as several months while attempting to retrieve their misdirected deposits.

As the result of the tremendous infusion of cash each month under a mandated direct deposit system, financial institutions would have the potential for reaping huge profits by investing funds before they were withdrawn from customers' accounts. It would be extremely helpful if the Federal Reserve Board would provide the committee with estimates of the potential profits flowing to financial institutions under a mandated direct deposit system for the major types of Federal recurring payments.

While AARP believes direct deposits can be an attractive option for receiving funds, it should not be the only option available to the consumer. We therefore view sole recourse to direct deposit as an unacceptable method for acquiring access to basic banking accounts or for receiving government check cashing services.

AARP appreciates this opportunity to present our view. We look forward to working with the committee toward passage of both S. 906 and S. 907 during the 101st Congress. Thank you.

[The complete prepared statement of Robert J. Sell follows:]

STATEMENT

OF THE

AMERICAN ASSOCIATION OF RETIRED PERSONS

ON

S.906 "GOVERNMENT CHECK CASHING ACT OF 1989"

S.907 "BASIC BANKING SERVICES ACCESS ACT OF 1989"

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

UNITED STATES SENATE

June 6, 1989

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Introduction

The American Association of Retired Persons (AARP) appreciates this opportunity to comment on S. 907, the "Basic Banking Services Access Act of 1989" and on S. 906, the "Government Check Cashing Act of 1989." We are pleased that the Senate Banking Committee is highlighting the issue of access to banking services through these hearings.

AARP supports both S. 907 and S. 906. We urge the members of the Senate Banking Committee to expeditiously act upon these important pieces of legislation, which will assure access to affordable banking services and a safe place to cash government checks for many low income and elderly persons.

Assuring the safety and soundness of depositors' funds has, understandably, been of primary importance to the 101st Congress. However, once depository funding problems have been resolved, AARP believes the Congress should make certain that all potential banking customers have access to affordable banking services. This action is essential to fully restore public confidence in the ability of the financial services system to respond to their most basic depository needs.

Basic Banking Accounts

Today, consumers still find themselves having to "jump through hoops" just to get badly needed banking services. Access to simple banking services is oftentimes difficult, sometimes virtually impossible. Financial institutions now charge for services they used to offer for free, and have increased fees on other services. "Initial Deposits", "Monthly Fees", "ATM Charges", "Minimum Balances", "Balance Inquiry Fees", as well as other terms and conditions are prevalent on many accounts.

Faced with this situation, consumers are having to budget for increased account costs, keep high balances, or give up bank accounts altogether. For many low and moderate income households, the increased costs of maintaining banking accounts have resulted in strained budgets. Others find it difficult to accumulate sufficient minimum balances while trying to meet necessary expenses like food, housing, and utilities.

The new or increased fees, coupled with more onerous account terms and conditions, have placed banking services beyond the reach of some low and moderate income, and elderly people to the point where they simply do not have bank accounts. For those without an account, paying bills becomes difficult, and personal safety is jeopardized.

Since many people need access to basic, no frills bank accounts, AARP believes Congress should require financial institutions to provide individuals with access to a minimal level of banking services.

Under S. 907, depository institutions would be required to offer checking accounts to individuals who have $1,000 or less on deposit. Fees and service charges for routine transactions could not exceed a minimal amount, as determined by the Federal Reserve Board. Minimum or opening balance requirements would be limited to $25 or less, with 10 withdrawals allowed per month. This account would not require the individual to exclusively use automated teller machines or other nonteller services, and would not require other account relationships. The institution would be required to provide either a monthly statement or a passbook detailing account activity.

Passage of S. 907 will assure the ready availability of basic, no-frills banking accounts for many low and moderate income people. AARP hopes the Senate Banking Committee will support the basic banking bill, S. 907.

Government Check Cashing

AARP is concerned that many financial institutions have adopted "If you don't bank here you can't cash here" practices. Often these policies extend to government checks, with some institutions refusing to cash federal government checks (including Social Security, pension, retirement and disability benefits), state government checks (including pension, teacher retirement, and public assistance), and local government checks.

People without bank accounts obviously have the greatest difficulty cashing government checks; however, even people with accounts are encountering problems. Many financial institutions require their account holders to maintain a balance sufficient to cover the amount of the check being cashed. Thus, if you get a $500 monthly retirement check, some institutions may require you to have a $500 balance on deposit to cash your retirement check at your own bank.

Tragically, many of these are low income people who need their available funds to meet ordinary living expenses. They simply cannot afford to forego timely access to their money. Those who cannot get their government checks cashed at financial institutions are relegated to cashing their checks at expensive check cashing services.

To alleviate this problem, S. 906 will require institutions to cash government checks. Financial institutions would be required to cash federal, state, and local government checks in amounts of $1,500 or less. In return, institutions could assess a reasobable fee, as determined by the Federal Reserve Board and based on actual cost studies. To qualify, consumers would be required to register for check cashing privileges with a particular financial institution.

AARP Opposition to Mandated Direct Deposit

AARP encourages its members to utilize direct deposit services. By arranging to have funds such as Social Security, government, and payroll checks deposited directly, consumers are able to receive their funds more conveniently and securely.

However, it must be recognized that different consumers have different needs. Thus, the decision concerning whether or not to utilize direct deposit services must remain with the individual. The individual must retain the prerogative of choosing the depository method that best suits his or her particular needs. To establish mandated direct deposit as a prerequisite for access to banking services is, in AARP's view, both unacceptable and inappropriate. AARP opposes mandating direct deposit as a necessary precondition for the receipt of a basic banking account or the use of government check cashing privileges for the following reasons:

* Many older Americans are reluctant to use direct deposit. In spite of aggressive efforts by the Treasury Department and by financial institutions to encourage direct deposit, only 47% of Social Security beneficiaries use direct deposit. Thus, over 20 million Social Security beneficiaries do not use direct deposit;

* Acceptance of direct deposit is lowest among the low income population. According to Treasury Department statistics, only 28% of Social Security Disability payments are directly deposited; only 14% of Supplemental Security Income benefits are directly deposited. Federal Reserve Board figures indicate that only 10% of families with bank accounts whose annual incomes are less than $10,000 use direct deposit;

* Consumers are experiencing difficulties in resolving direct deposit problems. An informal survey of our membership conducted through the AARP News Bulletin has revealed a large number of individuals who are encountering problems with the direct deposit of their Social Security funds. The greatest number of complaints came from people whose Social Security funds did not get deposited to their accounts in a

particular month. These letters did not indicate any unusual event involving a bank merger or takeover, nor were they able to lay blame for the mistake squarely on the shoulders of the government or the financial institution. Nonetheless, the result is that some Social Security beneficiaries have had to forego access to their funds for as long as several months while attempting to retrieve their mis-directed deposits. Other survey respondents encountered problems with direct deposit when they changed banks. Many of these people experienced significant delays in switching direct deposit from their old bank to their new one, with Social Security funds going to the old account months after it was closed. AARP has participated in an ongoing consumer work group with the Financial Managemant Service (FMS). While we applaud FMS's nationwide pilot projects aimed at perfecting direct deposit, we disagree with FMS on the issue of choice. FMS believes the government or banks should choose who receives funds via direct deposit; AARP believes the choice is best left to the individual;

* As the result of the tremendous infusion of cash each month under a mandated direct deposit system, financial institutions would have the potential for reaping huge profits by investing funds before they were withdrawn from customers' accounts. With over $18 billion a month paid in Social Security (OASDI) benefits, the potential industry "float" from the direct deposit of Social Security benefits alone could be staggering. Obviously, this windfall would be much greater if all recurring federal payments were subjected to a direct deposit requirement. It would be extremely helpful to this debate if the Federal Reserve Board would provide the Committee with estimates of the potential profits flowing to financial institutions under a mandated direct deposit system for the major types of federal recurring payments.

While AARP believes direct deposit can be an attractive option for receiving funds, it should not be the only option available to the consumer. After knowing the risks and benefits associated with direct deposit, the individual is best able to decide whether or not to receive funds electronically. AARP is strongly opposed to mandating direct deposit as a necessary precondition for services. We view sole recourse to direct deposit as a totally unacceptable method for acquiring access to basic banking accounts or for receiving government check cashing services.

Conclusion

AARP appreciates this opportunity to present our views. We look forward to working with the Committee toward passage of both S. 907 and S. 906 during the 101st Congress. Thank you.

Senator DIXON. Thank you very much, Mr. Sell, for your very interesting perspective and we will develop that in the question and answer period.

Peggy Miller, legislative representative of the Consumer Federation of America here in Washington is our final witness.

STATEMENT OF PEGGY MILLER, LEGISLATIVE REPRESENTATIVE, CONSUMER FEDERATION OF AMERICA, WASHINGTON, DC

Ms. MILLER. Good morning. It is a pleasure to be here, and I would like to say that I look forward to working with you in your new capacity as the new chairman.

If I tend to ramble on a bit on supervisory good will, please excuse me, but there is a piece of legislation over in the House Rules Committee today, and I kind of tend to move back and forth in my thoughts.

But we are here today to discuss check cashing, "lifeline" banking and community reinvestment. I would like to step back a minute before getting into the particulars of these pieces of legislation which Senator Metzenbaum has introduced and we support very strongly, and to try to draw a brief picture of how we are looking at the reasons that this legislation is before this committee today.

Deregulation has been moving along fairly well now for about a decade. You are attempting to craft a new financial system, actually, and whenever something like that is attempted, it achieves many positive and excellent products, which I think we can point to within this current system. There is an emphasis on competitiveness, there is an emphasis on price, and out of that, many consumers have been affected. But whenever something like that is being developed, there is always the fallout. There always is. You have to kind of step back every few years and say, all right, where are the problems from this? And I think that is why we are here today, because out of that system and growth of it, a lot of tuning is needed, and some of that tuning has to do with as the prices have been increased, banks had to start setting fees on every product, the profit margins have dropped, the competitiveness in the system is fierce.

Out of that, you have higher prices on all your bank products. And another result from that situation is that basically even the way they tackle loan products—it's not just your checking accounts and your lifeline situation, basic banking services—but also your loan products. It costs money to write a loan. Your labor, your loan officers. Moving the loan through the system. You look for the fastest loan product. You look to move things through with little labor. You look to package them simply. You look for simple equations, so that it will move through.

The fallout from that cost benefit attitude is, you have people who can't afford accounts any more. There is an elasticity in demand, and we have 16 million people without bank accounts now. They are having to go to check cashing outlets where there are very many complaints about cost and price gouging. Even though you have a whole development within our communities and our neighborhoods, where nonprofits are trying to take a look at new ways to deal with low income housing, such as limited equity packages and working with the cities and trying to put in sweat equity and trying to package things and come to grips with these problems, they are finding that they cannot get help or the time from their local banker. Why? These are very complex sorts of loans. They require time. They require reeducation of our loan officers and that costs money.

So all of that has dropped out of the system. On the whole, you do have some positive elements, in that a number of banks—from our position, we look at it more as about 25 percent of the banks in this country—are attempting to deal with problems of check cashing and lifeline banking. The reason our number is lower than ABA's is because we consider that a minimum balance requirement of $200 is too high. So if a minimum balance exists of $200, and they call it a lifeline account, in our opinion, it is not, because most of these people cannot maintain such a balance. We believe that around $25 is closer to an acceptable lifeline minimum balance.

So basically, from the positive angle, a great number of banks are trying. The trouble is, you still have a vast number that are not. And so when stepping back and looking at this situation, we say, all right, do you have the right then at this point, looking at deregulations, do we have the right to ask banks and thrifts to accommodate these concerns? Is there a public responsibility?

In our opinion, we answer with an emphatic yes. I think that the bailout from the S&L bill has reminded the public, has clarified a situation that has never been as clear before in the history of our financial system, that we are the backers of this financial system, of the federally insured financial system. The taxpayer and the banking customer are the ultimate backers. And for that reason, yes, they have a right to say that that system also needs to respond across-the-board.

What are the responses needed? First, the responses are needed in the check cashing field. In our opinion, there have been many points raised today in terms of direct deposit and problems of fraud.

I do always experience a small sense of outrage when fraud is pointed to in this area, because basically, the fraud that we witness in the current situation within the thrifts is extremely high and we don't even know the total amounts yet of that fraud. And we are talking here about highly paid bureaucrats in comparison to the fraud that is being pointed to, the worries of the banks in terms of checks coming across the counter.

We heard 1 million checks. Let's multiply that by the average size of a $500 Social Security check. We are talking $500 million. Look at the fraud we are talking about within the S&L situation?

So fraud alone gets me a little bit upset, because we are getting here into a differentiation, pure and simple. Connecticut isn't yet experiencing any of this fraud. We called 19 of the banks that cash government checks right now to ask them, do they experience fraud? The answer was "no", "when we trained our tellers in terms of comparing the signature to the check and the signature on the back of the check, there was no fraud." The fraud is negligible.

So that question is adequately addressed in the legislation.

On the lifeline banking situation, the only thing I would like to point out is basically our other concern is that the recent bill that passed out of this committee on the savings and loan crisis also increased the premium insurance fees. We did a study which we submitted to the committee at the time of markup that showed that every time you increase bank fees, they then, in turn, raise them from their account customers. And that 36 percent of such funds come from the small depositor.

In our opinion, the results of that bill means that the small depositor is going to bear 36 percent of the costs of those increased premium insurance fees, which will drive more out of the system.

So for that reason alone, we think it is extremely urgent to move the lifeline banking account program, because it will at least help to hold those people in. And our ultimate object is, and I am finalizing here, is we would rather bring back into the system those who are in the check cashing world. Yes, we think there is value, not only for them, because it is safer or cheaper, et cetera, but in addition, it is much more valuable for a stronger economy, stronger communities, teaching them how to save, and we would like to work with the community, in terms of trying to achieve that.

We think the bills that we are discussing here are the first step in that regard. Thank you.

[The complete prepared statement of Peggy Miller follows:]

TESTIMONY OF PEGGY MILLER, CONSUMER FEDERATION OF AMERICA, BEFORE THE SENATE BANKING SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS ON JUNE 6, 1989.

Mr. Chairman, my name is Peggy Miller. I am here today on behalf of the Consumer Federation of America, (CFA) an umbrella organization representing over 240 national, state and local organizations who in turn represent more than 50 million people in this country.

I look forward to working with you as the new Chairman of the Consumer Subcommittee. The subjects before us today, the Community Reinvestment Act, government check cashing and lifeline banking, are issues which CFA and many other organizations have worked on for years.

CFA supports the passage of Senator Metzenbaum's legislation on government check cashing, lifeline banking, community reinvesment and home mortgage loan disclosure. We believe that banks should be required to offer such services and provide lending information for the following five reasons:

** the fallout of financial deregulation policies must be balanced with encompassing programs that address the needs of those consumers who have been forgotten in the current competitive conditions;

** there is a crying need for creative community investment in housing and small business lending as witnessed by the growing number of homeless, housing peaks and valleys, steep housing prices and failing communities;

** complaints of price gouging in check cashing outlets continue unabated while only 25% of the banks in this country offer low cost check cashing and checking accounts;

** the entire economy would benefit, and thus all consumers, from a surge in community lending due to the domino effect of such lending on job development and thus on the tax base, improved attitudes, better education, more creative infrastructures;

** federally-insured depository institutions are publicly-backed enterprises with responsibilities to meet the needs of all the public, not just their major shareholders.

BACKGROUND/PROBLEM:

This is a particularly appropriate time to be holding these hearings and to reflect on the overall direction of our financial industry and its responsibility to meet the financial needs of all consumers.

The $300 billion taxpayer bailout of the thrift industry brought on by poor Savings and Loan (S&L) management, disregard for regulatory requirements, and simple fraud has clearly focused public attention on its direct relationship and supportive role vis-a-vis the federally insured financial system. The international negotiations on the bailout of overextended LDC's sharpen this distinction even more since the results of such negotiations may contribute to further FDIC insolvencies and consequent taxpayer bailouts.

I realize that the banking and thrift industry do not believe they should be considered a "public utility". Banking lobbyists have often stated that the banking industry is a private enterprise and should not be looked on as having to fill any given public purpose.

Such an assumption made in the face of the astronomical costs to the public of the S&L bailout is indefensible. Private enterprises put up their own funds and bare all risk. If their investment decisions are poor, they run the risk of losing all they have. The risk with federally insured banks and thrifts is clearly and ultimately borne by the taxpayer and banking consumer, and the industry is, therefore, not a true private enterprise. It has responsibilities towards its backers -- the public.

One must only review the history of the financial industry development to see the layout of a system developed to meet the needs of all consumers. The initial choice of developing a decentralized system with branches in all parts of the country was intentional. Such a system ensured that all people, rural and urban, would have access to their federally-insured banking services.

But this public responsibility is not being met adequately. In the last fifteen years, the sensitivity of the federally insured banking industry to the needs of all consumers has diminished greatly.

Deregulation may be providing a number of skilled financial technicians and wealthier individuals with the means to reap vast monetary benefits for themselves or their companies, but the majority of consumers, who have incomes less than $25,000, cannot afford brokers. They can hardly afford the minimum balance requirements necessary on most checking accounts if higher banking fees are to be avoided. Their problems are more stark -- they need affordable housing, small business loans, clear information about banking products and reasonably priced check cashing and bill paying accounts.

Financial deregulation has encouraged an amazing display of true competitive activity. We have witnessed the development of many new banking products which have provided many consumers with the ability to earn more money on their checking and savings accounts. There have been many benefits from such product development, but sadly, these benefits have only been shared by those of higher income. Those with less than $25,000 income have experienced a net cost to banking, and have watched affordable housing and small business loans dry up.

Their problems do not spring only from financial deregulation. Advancements in technology, urbanization, marketing, transportation developments, energy price hikes, diminishing resources and pure population growth all have contributed to these real problems.

Still, deregulation has encouraged a shift in the attitudes and practices of bank and thrifts and their holding company CEO's resulting in a greater emphasis being placed on product diversity, competition, the high deposit customer and overall profit margins, as well as high risk bond and real estate development by some thrifts.

Because the profit margins are so low in dealing with low and middle income consumers, companies often find it simpler to just exclude the service needs of these customers from their product and market development plans. The end results are simple: funds and technical attention do not flow in the direction of these low budget customers and they consequently find that the few financial products available to them lack creativity and are in short supply. Such is the case in the commmunity investment and mortgage lending area as well as the basic banking service area.

Meeting these needs is very possible. The banking industry needs only to alot a portion of the creativity they devote to complex third world debt problems to fill in these gaps in the banking system. Many banks and thrifts already have realized the need to expand their products and information to address low income and community banking needs. 25% of the banks in this country do offer lifeline accounts. 29% do offer check cashing services. A number of banks have agreed to employ creative community investment programs.

Still, bankers, for the most part, at least in this country, remain highly lacking in creative solutions to low income and community banking needs:

-- Most do not offer group housing loans, even though the housing crunch has required such new housing approaches for years.
-- Those wanting to package cooperative housing and business loans, limited equity housing loans, cluster housing/business development loans, sustainable agriculture loans, renewable energy loans and the like to meet evolving community and consumer tastes can find few bank loan officers that will give them a hearing.
-- Even though the one-earner, two-parent household is virtually a lost institution, most banks continue to hold to rigid 9:00 - 3:00 hours forcing lack of banking assistance and virtual sole use of ATM machines, even though elderly and low-income have been shown to be extremely reluctant to use ATM machines.
-- Few lifeline banking packages for low-income, and continuation in discriminatory requirements for account opening such as credit cards and high opening balances.
-- Little banking assistance for women and minorities struggling to understand the financial world and make use of it.

One out of five families have no bank account. Check cashing outlets that charge 3-6%, on average, to cash a government check have sprung up all over the country. 71% of banks refuse to cash checks for non-account holders, and 74% offer no lifeline banking service. Banking fees have increased dramatically and minimum balance requirements are climbing. Mortgage loan customers, desperate to lock-in a loan, are being offered new products that charge top interest rates in return for an immediate lock-in service. The homeless numbers are growing.

In addition, the lack of creativity and community concern has resulted in the stunted development of businesses and technologies that could assist this country's neighborhoods and communities to flourish, that could provide far more jobs, and has increased the polarization of the people in this country by income distinction leading to greater crime and political apathy.

The basic financial policies of our financial system direct the pattern of our everyday lives in far more ways than virtually any other infrastructure, and our current financial policies are short-sighted.

It is time for all our federally-insured banks and thrifts to meet their public responsibility. They must follow the example of those institutions who have been willing to "get their feet wet" and seem to be handling their broader responsibilities without major duress.

The great potential that is visible if our federally insured institutions were to choose a course that turned its focus back to the community, to the creative force of small businesses and new housing concepts, encourages many to keep driving for such change. Alternative low-income and limited income housing concepts continue to be refined by various non-profit housing organizations and small projects exhibiting this work exist throughout the country, funded by money scraped together and placed in revolving loan funds. Unique check cashing and lifeline banking programs, combined with education on financial accounts, are in various locations.

The knowledge gleaned from these programs is there for the picking and could be leveraged into a vast, creative set of community banking programs. This Committee could be of help in this regard by sending strong signals to our federally-insured banking system that such attention is needed and needed now.

CHECK CASHING:

The need for check cashing programs in our banks and thrifts continues to increase. GAO reports that 16 million families, one out of every five, have no bank accounts and, since only 29% of banks cash government checks, these people must go to food stores, or check cashing outlets. Constant reports of price gouging in check cashing outlets are submitted, as well as tales of having to travel 30 miles to cash a check, refusal to cash checks by banks of people based on their welfare status, and the like.

Last year CFA testified on this issue, at which time we summarized the results of our 1987 check cashing outlet survey conducted in 20 major cities, the New Jersey Public Advocate Survey, and the Consumers Union Survey in California all which investigated costs in check cashing outlets. Fees of 3-6% the face value of the check were found to be the norm, with prices up to 30% reported. In New Jersey's regulated check cashing outlets, regulations were ignored and overcharging occurred in 50% of the cases. Connecticut, due to a heavy complaint problem, passed legislation requiring banks to cash state issued welfare checks.

This year, Virginia reports similar problems. You have heard the testimony this morning of the VCCC who surveyed check cashing outlets in Virginia and found that their outlets were charging an average of 3% to cash a government check. We hope that their report helps to clarify the extent of the price gouging problem.

CFA supports policies like Senator Metzenbaum's check cashing legislation because we believe that low income people should not have to pay such high prices, because broader availability will ease the long-distance many must travel to cash a check, and by broadening the availability of low cost check cashing these consumers will be encouraged to enter a bank again. We take this position for several reasons:

--- Dealing from a cash position curtails a person's financial possibilities and restricts them to an endless position on the lower end of the economic strata. When operating with cash there is virtually no opportunity or incentive to save funds for future life crisis. In addition to the impact on these individuals, this in turn places a greater strain on the government to fund low-income assistance programs to fill these emergency gaps.

--- Since banks will not cash their checks, it places that "cash" consumer into risky, often exploitative situations where they are forced to pay extremely high prices just to cash their checks. The goal of social security, Supplemental Security, Aid to Families with Dependent Children, and other such programs is to provide financial assistance. Decisions on the amount of such assistance are based on long, difficult debates in Congress and often become razor thin lines to fill nutrition requirements and other basic poverty guideline requirements. No one, to my knowledge, has been factoring in the loss of 3-10% of these funds to a new industry of check cashing owners. Therefore, these people are suffering undo hardship based on these high prices they must pay to cash their check.

--- They must carry large sums of cash on hand at certain times, making them easy targets for assault and theft. (This is a particular problem for women and elderly.)

--- And a cash position makes bill paying a difficult, time-consuming and costly activity taking the person away from work just to pay their bills, which is burdensome to the individual and,in turn, is an expense to the company also.

Senator Metzenbaum has been a creative, tenacious supporter of change in this policy area. His legislation would be a first step in providing a safe, low cost check cashing option to low-income, non-account holders.

The reasoning behind the decision by so many to operate without a bank account is not completely clear. The American Bankers Association published a report in 1985 of survey results which indicated that roughly half of those without bank accounts now once had a bank account. Those who once had a bank account reported that they had dropped it because they found they "did not have enough money to make it worthwhile".

Though it appears that half of the check cashing population has no bank account due to lack of funds or perceived lack of funds, the reasons for the other half operating in a cash society are less clear. Reports of discriminatory treatment and burdensome, sometimes exclusive account requirements, such as credit card identification to open, high opening and minimum balance requirements, by certain banks are mentioned. The shortness of the banking hours for those working a full five-day week, the immobility of some consumers, and the lack of proximity to a bank by the low-income customer are factors that play a role. Some simply do not trust bankers.

To endeavor to draw these consumers back into the bank lobby, so they would have a safe, inexpensive means to cash their check, we support a simple, clear mechanism: requiring banks and thrifts to cash checks for a low fee.

Problems of fraud:

Banks and thrifts claim that such a check cashing requirement would be a clear inducement for rampant fraud. They say that bad checks would proliferate.

FRAUD? They claim fear of the fraud that could take place from the poor passing bad checks over the teller counter, when over $100 billion has been looted in a few short years from Savings and Loans due to the fraudulent scams of highly paid insiders and their racketeering friends?

Even so, in 1988, CPA did call 19 banks who currently cash government checks in an attempt to learn more about fraud experiences. The response was the same. When the teller was trained in comparing signatures of the i.d. card to a signature card on hand, fraud was eliminated.

Connecticut has operated since January under their new check cashing requirement, and, as of yet has detected no great upswing in the numbers of bad checks as a result of their new law requiring banks to cash government checks. Furthermore, the long lines that were reported by those banks who once were the few to cash government checks have been eliminated by the expansion of locations -- another positive result that should be noted.

We believe that the provisions within Senator Metzenbaum's legislation regarding the 20 day hold allowed to verify identification, the general identification requirements, and the limitation on the location of acceptable checks, as well as the provisions enabling the institution to drop any customer that shows a pattern of fraud, adequately address the problems of fraud that might unfold. These provisions were hammered out during markup of the House Banking Committe version of the Bank Deregulation bill last year, and seemed to satisfy the banks concerns at the time.

Issue of Direct Deposit/Electronic Funds Transfer:

CPA is very interested in the constant developments within the entire electronic funds, information and products transfer industry. So many electronic fund transfer products are being tried around the globe, it is impossible to know which products will ultimately succeed in gaining market share.

We are told of point of purchase, point of sale, and debit cards, as well as simple direct deposit/ATM systems. New hardware and software to advance home shopping could be another arm of this embyonic industry.

It is difficult at this time to guess where it will all lead and which technologies and debit systems will finally emerge as the winners in the growing competition. It is difficult to even say whether these systems will be of advantage overall, once the entire socio-cultural-economic factors impacted by such developments are taken into consideration.

It seems a bit early to even consider mandating one of these possible systems on the low income and elderly check cashing population, namely, direct deposit.

First we would have to overcome real hurdles in terms of combatting functional illiteracy, stubborn lack of interest in direct deposit exhibited by low-income and elderly, long-engrained cultural traditions related to the "check in the hand, trip-to-the bank", lack of mobility problems, massive dislocations of,albeit costly, but workable cashing systems, lost check transfers, and the increase in ATM fraud, in order to get these consumers to use such a system properly and without too much penalty.

I have serious doubts as to how we would, on a national basis, economically manage to overcome such a list of complex roadblocks without serious deprivation to many during the process and after.

Then we must take into consideration that fifteen states do not allow direct deposit at all.

Even if we could accomplish this change of government checks to a direct deposit system, we may find that as soon as we have spent millions in implementing the conversion to one system that another has won the competition and our new infrastructure has become obsolete.

The more prudent course might be to address the problems associated with check cashing now through a bill like Senator Metzenbaum's, to encourage banks to offer a second approach: free direct deposit/withdrawal. Such an incentive would induce many consumers to begin to shift towards direct deposit without such cataclysmic events as would be witnessed if direct deposit was mandated.

Regulation of check cashing outlets:

CPA does not suppport the federal regulation of check cashing outlets at this time. This would require establishment of another costly bureaucracy, and we seem to have difficulty funding and managing our current federal banking regulators as it is. Since we already have a bureaucracy in place to exam and manage our federally-insured deposit institutions, it would seem more in order to simply require these institutions to cash checks for a fee set by the Federal Reerve Boards, and to expect our current regulatory staff to conduct oversight.

LIFELINE BANKING:

Lifeline banking becomes more necessary with each passing year as we witness the constant increase in bank fees. The recent S&L legislation passed by the Senate and House Banking Committee will seriously aggravate the cost of banking for small depositors due to the sharp insurance premium increases in the legislation.

CPA analysis shows that increases in bank operation costs are passed on to the banking customer in a disproportionate manner. In fact, we expect that 36% of the increase in insurance premiums in the S&L bill will be shouldered by households with incomes less than $25,000, the small depositors in the bank, if past pass-through trends continue.

These customers have been considered expendable for the most part and have had a net cost to banking in the last few years as opposed to the net yield to banking experienced by those with higher incomes. These individuals enjoy the higher interest rates on checking and savings accounts that are available to those able to maintain higher balances.

If such a pass-though prevails, bank fees will increase sharply for small depositors and many will drop from the banking system. The only way this can be prevented is to require banks and thrifts to offer lifeline checking accounts.

Currently, CPA statistics based on our annual bank fee survey show that 74% of the banks is this country do not offer a lifeline account. GAO statistics in a 1987 report on bank fees indicated that only 15% of the banks in this country offer lifeline accounts.

CPA defines a lifeline bank account to be one that has the ability for ten withdrawals, requires no more than a $25 opening and minimum balance, does not require sole use of ATM machines for withdrawals, costs no more than $3 dollars total on a monthly basis and does not require discriminatory identification such as employment or credit card identification in order to open the account.

We take such a strict stand on the definition because we have found that unless you define your definition of a lifeline account when conducting bank surveys, that it is virtually impossible to get a clear answer as to what is available. Furthermore, the ten check definition and minimum balance issues are critical since these are two usual ways that confusion can set in on actual availability of lifeline accounts.

The American Bankers Association claims that 53% of the banks in this country offer lifeline accounts, but they do not define their term. When reviewing the statistics, there is a conflict found among the different tables upon which this statistic is drawn. The minimum balance requirement for many of these "lifeline" accounts is over $200. This is simply too high. Many people must draw their accounts down to virtually zero each monthy in order to survive. If hidden fees trigger at any such higher level, then low income people cannot afford these accounts since they will constantly be triggering the application of the hidden fees.

Many accounts called lifeline offer only 6 checks within the set low fee. We feel that this is too low a number for it does not cover basic billpaying requirements.

Senator Metzenbaum's lifeline banking legislation offers a reasonable approach to this problem. It would require all banks and thrifts to offer lifeline bank acocunts for a fee to be set by the Federal Reserve Board. The fee must reflect costs based on actual cost studies.

We support the use of actual cost studies because the only other mechanism for judging cost at this time is the functional cost analysis. This form of cost analysis is very general and is based on subjective judgements of the individual bank personnel. It reflects no accurate judgement of costs, as an actual cost study would reflect. Therefore studies would need to be performed by the Federal Reserve Board in order to make a determination of the costs of providing lifeline banking and check cashing services.

Check cashing services alone do not address the problems related to lifeline banking needs. Since our goals are to involve as many consumers as possible within the banking system, we wish to encourage a change to lifeline accounts from check cashing arrangements. Therefore both systems serve a purpose.

We also support consideration of curriculum development on use of bank accounts, money markets, and other financial investment products to be offered in our grammar schools, as well as our vocational schools.

COMMUNITY REINVESTMENT ACT:

Disclosure of community investment lending practices would help to provide local organizations and individuals with a more accurate reading of the lending patterns of their federally-insured depository institutions. The availability of such information will allow individuals to track the activities of their banks and thriftsd. This accountability to their community should encourage banks and thrifts to have more sensitivity to local needs as well as acting as another safety and soundness enforcement mechanism.

Disclosure of the Community Reinvestment Act (CRA) evaluations and subsequent CRA ratings that are made by bank and thrift examiners is necessary to encourage a greater attention by the examiner to the exam process and the rating process as well.

Virtually every bank in prior years has been assured a passing CRA grade by its examiner. Disclosure of a written evaluation as well as the actual rating received should help to discourage this cavalier attitude towards the process.

The current structure of the law which requires that an institution receive an acceptable CRA rating before its applications for various additional activities can be approved has been somewhat effective in those local areas where active community organizations have protested and demanded more sensitive attention to the community investment standards of its local banks.

Disclosure will place a proper emphasis on the examination phase. The emphasis on the application phase in current law must be retained so that the triggering mechanism exists within the system providing for a double check.

The CRA disclosure language in Senator Metzenbaum's legislation, which is very similar to that passed last year in H.R. 5094 is the preferable disclosure language.

It is particularly important that the evaluation and the rating be disclosed. The rating should be public knowledge. There is no reason that the community investment record of the bank or thrift should be withheld from the public eye. By disclosing the rating, the examiner will be held more accountable for the process undergone. Though we realize that this places the examiner in a more delicate position, we feel that it is the only way to strengthen the process laid out by CRA.

CRA is a particularly well-crafted piece of legislation because of its inherent flexibility to community lending needs and conditions. This flexibility also places the examiner in an even more difficult position though, because nothing is really spelled out and they must make a number of evaluations and final decisions that can have a serious impact on the bank's application approval process.

Therefore, CFA recommends that examiners receive even greater training in community investment evaluation processes. Currently the Office of Regulatory Activities of the FHLBB has started a school for consumer compliance which seeks to provide improved training in consumer compliance and CRA exams. Such a school is needed for all examiners so that they feel better equipped to handle the pressures and constraints of their position.

CFA wishes to see the rating structure approved also so that passing grades will not continue to be the given outcome of all examination reports.

Senator **Dixon**. Thank you, Ms. Miller. Again, we will have a 10-minute limit on the questions, and I will begin the questions.

Mr. Stevens, you were talking about this percentage business, and of course, one of the things I have already learned, everybody has got a percentage around here. But frankly, your percentages are pretty high on the amount of lifeline banking service and the amount of check cashing notwithstanding the absence of an account, if your figures are correct, and I have no reason to dispute them.

Now just to be the devil's advocate here, assume that your numbers are correct and assume that this much service is already really being offered out there by the banking community. And frankly, I think the consumer groups dispute those figures. But assume it. Now then, Mr. Loundy has talked about the fact that there is already at hand some statistical analysis of the cost of cashing a check and the cost per month of the account and things of that character. And assume that the cost of fraud as an institutional expense, even though my friend Ms. Miller might take issue with it, can be established. Now then, what is the final resistance of the institutions themselves to suggesting that everybody ought to participate, not that I have this, you know, empty adherence to the idea of 100 percent of everything, because I don't think there is 100 percent in much of anything, but why would you have a problem then, aside from the philosophical argument that we always have around here about Government intervention, in some involvement where we would say to people, look, you know, why don't you cash these checks? We are going to let you make a little profit. We are going to see that there is no problem with fraud. You guys are saying 90 percent of you are doing it already, or whatever the number is, so what's the problem?

CHECK CASHING

Mr. **Stevens**. OK. If I could, Senator, I think there are two concerns here. One, as you say, the numbers are different. I would note, in Peggy Miller's written testimony on both page 1 and page 4, she cites numbers about the number of banks offering low cost checking and cashing checks and also on page 4, you know, it talks about banks not doing it and offering no lifeline bank service.

The problem we have is the criteria established. If we come to a narrow criteria for who has a low cost account, we run into these kind of problems with the numbers. The criteria, as I understand it, that the Consumer Federation adopts for low cost checking, $3 a month charge, 10 checks free, no minimum balance to open, less than $25 to open, no minimum balance to trigger an extra charge, and free ATM use are, as I understand it, their criteria.

Now my bank offers a $2 a month, 7 free checks, but we don't qualify, because we don't provide free use of the ATM.

Senator **Dixon**. But can I argue with you a minute, Mr. Stevens?

Mr. **Stevens**. Sure.

Senator **Dixon**. Respectfully. This isn't a question of haggling about price, as we used to say in the old days. Assume now, again I want to get back to the basics. Assume we could establish what the industry itself saw as a fair number on the cashing of a check—Mr.

Loundy gave a number for my State, and he said the number was 33 cents a check, and the number for the month was $5.07 a month. I don't know if that even takes in account protection against fraud. It is a matter we could establish. Now when you get down then to that, now then I am asking you, is that still a thing just because of the philosophical quality of it that bothers you, when 90 percent of you are doing it anyway, if your numbers are right?

Mr. STEVENS. The problem with that, Senator, if I may, is that everybody now has the set way of doing it.

Senator DIXON. Sure.

Mr. STEVENS. Everybody's costs and every community's needs tend to be different. There is, in my judgment, no set way to do this. What we have, I believe, works real well at the Bryn Mawr Trust Co. in suburban Philadelphia. Now there are easily a dozen other alternatives readily available in our community with various features to their account. You can get more free checks, and so forth. The thing we object to is setting a standard to which everybody will instantly adhere. It may be right for some and wrong for others.

Senator DIXON. Well, OK. I don't want to be a bother to you about this, but could I pursue this sort of assiduously with you for a moment, because while you used to be in Waukegan, you are a Pennsylvania voter now and if I offend you, it won't hurt anything. I've got to be careful with Mr. Loundy and Mr. Sell, because they will vote in the next election. [Laughter.]

Mr. STEVENS. My mother and dad are still there.

Senator DIXON. Oh, I forgot about that! Your mom and dad. [Laughter.]

Well, I'll treat you kindly, so I don't lose their votes.

Look. Here is what I am trying to say. If Mr. Loundy is right, there is a book like the one he's got in his right hand for every district in the country. Now I am going to look into that immediately, and if there is, there is a price in every district in the country. Now let me extrapolate from that and see if Mr. Kelly is right, in addition to that, inside the system there are differences in the minority banks with the lower accounts in the inner city, and I hear that as well, but I get back to the fact that apparently there is some place at which people of good will could find a number that is probably acceptable, that we would say to you, look, OK, Mr. Loundy said you're not public utilities. OK. We concede you are not public utilities. You are in business to make a profit. We recognize it. Now, so you are not a public utility, and you are in the business to make a profit, but look, cashing a check costs so much, and at this level, you will make a profit, and fraud is so much, and at this level you are protected. In the inner city or someplace with the numbers lower on the accounts is the difference of all that. Now then I come back to this. Then is it still a problem?

Mr. STEVENS. Well, Senator, we would be happy to work with you to try to come to some resolution of this kind of an issue.

Senator DIXON. Well, you know, let me observe this, and I don't want to be a smart alecky guy, when I say you understand this issue isn't going away.

Mr. STEVENS. Yes, oh, yes. I understand that clearly.

Senator **Dixon**. I have been here a long time now. My friend from Ohio is resolute. We live with this man. He is here forever. [Laughter.]

He's not God, but he will be here a long time. [Laughter.]

Mr. **Stevens**. One of the things that will happen because we do, in fact, cash checks for nondepositors, we cash government checks, assuming we can satisfy ourself about the identification, local checks are not a problem for people. We don't charge them for it.

Senator **Dixon**. I understand.

Mr. **Stevens**. A new rule will mandate a charge for them.

Senator **Dixon**. See this?

Mr. **Stevens**. It looks like an ID with a picture.

Senator **Dixon**. Well, that's my driver's license. It's got my picture on it. It's not that bad a picture. [Laughter.]

It's got my Social Security number on it, and it's got my signature on it. Now the fellow from Connecticut, the commissioner, said they require another card as well, as I recall. I don't know whether that is so important, but that is another question we could look into. If you could make a modest profit, and if you were protected against fraud, and if you complied by saying that a person had to have one of these and show it to you, I mean, what's the big deal after that?

Mr. **Stevens**. If I may, the concern we have about that is that you now have mandated precisely what is required in order to get a check cashed by law. Right now, if you come into our bank to cash a check that is fraudulent, you run some risks, because you are not entirely confident about questions are going to be asked about you, and we have people who have been around for a long time who have a great sense, if you will, for when they are going to get beat. They really are very good at it. And because that discretion is exercised, I think is partly the reason you see the low fraud numbers that you have. There is discretion in the hands of those cashing checks. Once you write the book and you describe precisely what is necessary to do it, there will be a lot of people who will get busy to figure out how to beat it, one way or another. Brand-new ways will be thought up. And then we will be in that constant tension of standing up to the letter of the law, but being whipped because we know it is there.

COMPETING WITH BANKS

Senator **Dixon**. One of the other points that you and Mr. Loundy made that had some appeal to me is that there are all kinds of people out there competing with you that aren't banks. I don't want to return to the famous nonbank bank debate at this point, Senator. [Laughter.]

We don't want to do that today. But I think there is a validity in that that requires our attention. There are a lot of people out there competing with you that probably are not contemplated by this bill. I think that is what you are saying. And I would like to have from either one of you your expressions of the kinds of people you are talking about in that regard. You mentioned some of them, but whatever you could do to help us in that.

Mr. LOUNDY. Well, the check cashing situation, we are aware of the nondepository associations which we are generally here calling currency exchanges, but it includes the major food stores in the Chicago area. Jewel and Dominick's are the ones I am familiar with. I am sure there are others. Many gas stations will do it on a certain kind of basis. Some with charges, some with no charges. Some, as you had indicated, would build it into the cost of the product they are selling, and things of that sort.

In the CRA, we have a whole different situation where you have Merrill Lynch and insurance companies taking deposits into their money market accounts and investing in wherever they choose to invest and don't necessarily give the same kind of mortgage requirements and service to the communities locally. No CRA application there at all. In different areas, there are different competitors—Sears has been going into it for a long time out of South Dakota. Citibank is all over the place—in all different forms and corporate entities. Some are covered by regulation and some not. And that is what we are concerned about.

Senator DIXON. Well, I might just make this conclusion, because I see the red light applies to the Chair as well as anybody. But you know, one thing I suspect. I suspect that we ultimately would do something in this regard as an example. You and I understand what the currency exchanges are. We are familiar with Illinois. I suspect most people will still cash their checks in those places in certain parts of the city, notwithstanding the laws we pass, simply because there won't be other financial institutions going in there, and it is the only place at hand to do it. I think probably the only thing that might happen is that prices might go down for the charges in those institutions, simply because there is a viable alternative, but I could be wrong about that, but I am just thinking out loud about how those just might be the end results of this.

What do you say to that? And then I will be quiet.

Mr. LOUNDY. Well, you are getting back beyond the nonbank bank argument. You are getting back to some of the basic branching in arguments back to the days when Gale Cincotta sat here with us at great length. Generally, the proof then was that the underbanked areas were not substantially underbanked. They were populated then by the community banks. It was the major branching center banks that closed up their branches, and we are back to playing an old record again, Senator.

Senator DIXON. Well, I thank you. I believe if it is all right with the Senator from Ohio, this time I will move over here and let the Senator from Missouri ask questions first. The Senator from Missouri.

Senator BOND. Thank you, Mr. Chairman. Ms. Miller, there's nobody in the Senate more concerned about savings and loan fraud than this Senator, and I think that this committee has taken some pretty strong steps by increasing the penalties for fraud. We share your outrage at the instances of fraud which were perpetrated on the Savings and Loan Deposit Insurance System, and we intend not only to tighten the penalties but provide the resources to go after them. But certainly, I don't think that you meant to argue that because there has been grand larceny in savings and loans, you are not concerned about Mr. Kelly's problem with the fraud that he and his national banking members face.

How do you respond to his concerns, if we had some of the mandatory check cashing programs that you have endorsed?

CONCERNS ABOUT FRAUD

Ms. **Miller**. I didn't mean to argue that we didn't think fraud is always a concern, it is just sometimes I get a bit tired when I see the strength of their ability to get regulations, et cetera, and in this case, when we are dealing with a low income clientele that has a lot of problems, it is very difficult to get them addressed. But in terms of fraud, how do we think that they are addressed within the legislation? Basically, within the legislation, there are ID requirements, there is language which allows a bank the discretion—one of the things that we felt was very important to protect their ability to use discretion, so that if there is a justifiable reason that they believe that the check is fraudulent, they can reject it. Clauses of that nature. If there is a fraudulent pattern at all. If a person has bounced a couple checks or in terms of the lifeline banking language, any pattern of fraud whatsoever, they can immediately.

We think those sorts of considerations which were hammered out on the House side last year and these bills were passed there, and in fact, the check cashing bill was attached to Chairman Proxmire's last move to try to get deregulation through last year, it moved to the Senate floor.

So these things were fairly well hammered out. I feel that more because we don't have enough other evidence except fear of—Connecticut's not yet experiencing increased problems. In Ohio, they tried a project where they, for a year, watched to see if fraud would be a problem in Summit County. There was no problem. The banks that are currently cashing checks are not experiencing this problem. Because of that and because the need just keeps becoming—we think that there is enough reason to go ahead and try, and even in the language, the fee was the final argument, and the language is based on actual cost studies, but the cost is to also reflect fraud. So they are covered from that standpoint. And I just think because of all of that, all we are arguing about is a potential fear rather than any facts.

Senator **Bond**. Thank you. Mr. Sell, you heard in the previous panel, Mr. Douglas from the Treasury, talk about their experience which he cites that they are 16 times more likely to have problems with misplaced checks, misdelivered checks, if a Social Security recipient is getting a check rather than electronic funds deposit. Do you quarrel with those? Do you disagree with those figures? Does your membership feel that they are inaccurate?

Mr. **Sell**. Senator, we have no reason to disagree with those figures. I have no basis for disagreeing with them.

Senator **Bond**. So you would agree that the electronic deposit really does give greater protection and, in fact, is more likely to keep the Social Security recipient from having a check stolen or having to cash a large check and walk home with a wad of cash, thereby becoming potentially a target for robbery?

Mr. SELL. Well, we have supported direct deposits. It is simply that we do not believe it should be mandatory.

Senator BOND. Is AARP doing any major efforts to inform or educate these people, your members, on the benefits of direct deposit?

Mr. SELL. We have in the past. I don't know of any ongoing thing at the moment.

Senator BOND. Mr. Stevens, I was interested in your thoughts and Mr. Loundy's thoughts on the program— Mr. Douglas indicates that they are running a test in Baltimore on direct deposits and ATM withdrawals. And Mr. Kelly has advocated the electronic benefits system.

Is there any reason why your member banks wouldn't take direct deposit and make it uniformly available, if any citizen receiving government payments agreed to a direct deposit, outside of a proven instance of fraud or somebody who has forged checks?

DIRECT DEPOSIT

Mr. STEVENS. We certainly, and I said so in the testimony, support electronic transfer of benefits to people and would be more than happy to try and work toward some reasonable way of doing that. The concerns we have are a result that winds up with some of our customers subsidizing others. That would be a difficult thing. And a way from that, I think we would be perfectly happy to work toward a solution in that regard.

Senator BOND. Mr. Loundy.

Mr. LOUNDY. I think that anything that increases direct deposit would probably be a very positive step, and for my own purposes in our bank, we encourage it at all times, and I believe our association would support something that was worked around that.

Senator BOND. Mr. Sell, to come back a minute, you cite that AARP opposes mandating direct deposit. Your last reason is that "as a result of the tremendous infusion of cash each month under mandated direct deposit system, financial institutions would have the potential for reaping huge profits by investing funds before they were withdrawn from customers' accounts."

What is wrong with a bank or financial institution making a profit, if the consumer has access immediately to the funds, could walk up to an ATM and draw the whole thing out at once, if he or she wished, and if that direct deposit, the presence of those funds would lower the cost to the recipient who uses direct deposit, so that they don't have to pay a $3 fee for getting their check cashed? What is wrong with profit?

Mr. SELL. I don't know that I can cite anything that is definitely wrong with it, but I think it would be interesting to know how great a windfall that would be under the circumstances.

Senator BOND. I think you would probably have to be able to come up with some assessment of how long it would take the average recipient to draw the money out of the ATM's and, if they drew it out all at once, the profit would be very small. If they drew it out on a regular period—periodic withdrawals, it would be much greater. So I think you have to make a lot of assumptions that are pretty tough to make.

Mr. Kelly, I would like to ask you to respond to some of the questions raised by Mr. Sell and Ms. Miller about direct deposit. How could we resolve some of these concerns, and do you think we can work on resolving them satisfactorily?

Mr. KELLY. I would be very positive that we could, Senator. I think you would want to broaden it and not just say direct deposit, but include in that point of sale and ATM's. Personally, I was involved as president of a minority bank in Indianapolis in introducing a debit card system. Basically, we were reaching out to noncustomers. We wanted people—we were a small institution. We thought we could reach people who weren't customers of our bank. So we offered them an ability to access their money by establishing a line of credit. They wouldn't have to have a checking account with us, et cetera. And we wound up having 300 merchants in the city of Indianapolis and a large number of new accounts and customers, because it was a convenience item. They could walk into a merchant and make a purchase by having it debited to their checking account, or if they didn't have a checking account with us, their credit line.

Senator BOND. But the money would still be direct deposited in the bank? They wouldn't be having direct deposits to a supermarket?

Mr. KELLY. No, no, no. No. The money would be on deposit in the bank, but when they accessed it, they would make a telephone call, the merchant would, get an authorization code, and that transaction would be credited to the merchant's account there.

Senator BOND. One final question. You have got to have the pin number separate.

Mr. KELLY. Right.

Senator BOND. Do you run into problems with low income or perhaps elderly not being able to remember their PIN number on those ATM's?

Mr. KELLY. I could see that if someone had a problem remembering their number, but they could always, you know, find out what their number is, or you just create a new pin number for them. The advantages from a safety standpoint, and the fact that they don't have to walk around with a lot of cash. The real world is that there are people out there who know when these checks are coming in. They wait outside of check cashing places. They rip open mail boxes. I mean, that is the real world. So you could offer to the consumer a method of delivery where they don't have to deal with cash. They can go to a merchant. They can make their purchases, and that is taken care of. If they want $25, they can get that. They don't have to walk around with a lot of cash. They don't have to stick it underneath their pillows. They don't have to worry about going to their mail boxes and getting these things. Now that is not true of the whole country, but some of the areas where the fraud problems are great, those are the problems that people are encountering.

Senator BOND. Mr. Chairman, my time has expired, but it looked like Ms. Miller wanted to comment on that.

Senator DIXON. Let her do that.

Ms. MILLER. Thank you. We are increasingly interested in the developments in the electronic transfer field, and in light of the different potential out there, this is a massive field that is growing. And one of the things that we feel there is a need to continue the pilot projects like FMS explained this morning, that type of pilot project, in terms of all the ramifications from the positive side and the many uses of not only ATM machines but point of purchase, et cetera, and then how do we educate people in the use of those? All the problems too. I think that needs to continue. I think it needs to continue in various cultural settings. Our major concern which we think somehow can be dealt with because, you know, we just approach things that way.

But one of the major problems has been the functional illiteracy issue, and we have been trying to look more into that question because we suspect that like the statistics that AARP has on only half of the Social Security people use direct deposit, the other half doesn't. As you go down the income ladder, you do get into areas of very strong percentages of functional illiteracy. This is a big problem, when you are trying to move them into an entire electronic era, and that, in addition to the major problems of some elderly, in terms of remembering and getting them totally reacquainted, we suspect that we can do this, but over a very long period of time, where you really have to investigate a lot more thoroughly before a massive shift in this direction. But we would like to work on more projects of that nature.

Senator DIXON. I am almost tempted to observe—I don't want to be offensive about this—it would almost be better for them, if we could provide a good protective system though.

I want to go to the Senator from Ohio, it is his turn, but would you think about that observation, because it seems to me that those are the very people who get ripped off the most. You know, the illiterate people. I am shocked to say that my understanding is there are almost 20 million of them in this country now. There must be an awful lot of abuses of them out there, when they are walking around with checks or cash in their hands. I don't mean you should deprive them of it, but if you had a safer system, it might be a sounder policy.

The Senator from Ohio.

Senator METZENBAUM. Mr. Chairman, I go away from this committee hearing this morning with stars in my eyes, because I know of the pressure in this Congress to find additional sources of revenue to balance the budget, and as I sat here this morning, I was not alone thinking about check cashing but the unbelievable amount of unearned profit the banks have by reason of the float in the electronic transfer of funds.

Mr. Stevens, based upon your own knowledge as a business person, as a member of the board of the American Bankers Association and as a knowledgeable human being, what would you guess is the average float for government checks that are deposited in the banks of this country?

PROFIT FROM FLOAT TIME ON CHECKS

Mr. STEVENS. Well, we heard from the gentleman from the Treasury this morning that if there is a paper check sent, there is about a 3-day float, as I recall his testimony. If there is an electronic transfer of the money, the money is available that day.

Senator METZENBAUM. Sure, the bank gets it, but that doesn't mean the individual gets it.

Mr. STEVENS. The individual has access to it.

Senator METZENBAUM. I am not talking about access. I am talking about how much are the banks' gains—a Social Security recipient has a transfer made into a bank. It is an 87-year-old person. It is cold outside. It is raining. Doesn't walk down to take his money out for 2 days or 5 days or a week.

My question is, it seems to me that we are not talking about a little bit of money. We are talking about billions of dollars of float.

Mr. STEVENS. That's right. I liken it to my own mother and dad back in Waukegan, who are in their eighties, and their money goes to their account at the local bank, and they can call up and know that it is there, and it begins to earn interest on the day that transaction occurs.

Senator METZENBAUM. Not for all the accounts, Mr. Stevens.

Mr. STEVENS. They have a choice about where the money goes.

Senator METZENBAUM. Your parents are knowledgeable people. Their son is a prominent banker.

Mr. STEVENS. Well, that's true.

Senator METZENBAUM. But the fact is, the average person doesn't have an account. When you talked about all those people having accounts, I might say to you that the GAO indicated that their figures include all the banks in the country. When you talk about urban banks, it is a totally different picture. So that in urban areas, across-the-board, people don't have as many accounts, particularly welfare recipients, the poor, the minorities.

Now I am sitting here, and I am saying, the check comes in on Monday. Lots of people don't go there until Tuesday, Wednesday, Thursday, Friday, Saturday. How much is this worth to the banks of this country, the billions of dollars of float that is out there? You could put in your own account, but not all people do that.

Mr. STEVENS. Right, and if they hold the check, the check is mailed to them and they don't get to a check-cashing——

Senator METZENBAUM. I understand that. But let's talk about the money in the bank. Never mind the——

Mr. STEVENS. But the money in the bank is all there at the discretion of the deposit holder.

Senator METZENBAUM. Mr. Stevens, I would like you to have the American Bankers Association provide this committee with some information concerning the amount of the float with respect to which they are paying no interest and is sitting in the banks and is a pure gift to the banks.

Would you do that, please?

Mr. STEVENS. We will do our best to respond to your question, Senator.

Senator METZENBAUM. If I don't get it this way, I will get it another. [Laughter.]

Senator METZENBAUM. Mr. Stevens, tell me the distinction now. If I have a card and I go into bank and it has the name and the picture and all that on it, why couldn't you do the same thing and have the same kind of card—my question is—I withdraw that question. Let me restate it.

How does the person who comes to the bank get their money out today, when it is an electronic transfer of funds? How do you know that person is John Smith instead of Peter Jones?

Mr. **Stevens**. They either bring in a check, their own check, or they go to the ATM and use their personal pin number and can withdraw cash from the bank.

Senator **Metzenbaum**. If they don't have an account, they don't have a check. They wouldn't have an ATM account either. I'm John Smith. I've got $627 in my Social Security check. It was electronically transferred to the bank. Now I walk up to the bank, and I say, I would like the money that was transferred. How do I get it?

Mr. **Stevens**. We are talking, I think, Senator, about a new program, because there is no way to do that now, absent an account at the bank.

Senator **Metzenbaum**. Oh, the electronically transferred amounts all go into the bank where they're——

Mr. **Stevens**. They would go into a bank account in a bank of some sort, either interest-bearing or not, according to the recipient's choice.

Senator **Metzenbaum**. That answers that.

Mr. Loundy, you say you don't think that enough people are having problems cashing their checks to warrant Federal legislation. It was you who actually used the GAO's figure that 86 percent of the banks cashed Government checks for noncustomers.

Mr. **Loundy**. That wasn't my figure, sir. That came from Mr. Douglas, I think, or Mr. Stevens. I'm sorry.

Senator **Metzenbaum**. OK. Anyhow, whoever's figures they were, I questioned the GAO about those figures at last year's hearing on check cashing. I wondered how GAO could have such widely different numbers than the Consumer Federation of America. CFA figures have shown that more than 70 percent of the banks in this country don't cash checks for noncustomers. Here is what GAO said when I challenged them.

> Now you asked Senator Metzenbaum how the statistics from consumer groups differ from ours, and we think we would agree with Senator Metzenbaum. The studies the consumer groups did focused mostly on urban areas, while ours was a valid national sample. So we were picking out banks not only concentrated in urban areas but in suburbs and rural areas too. It is certainly our impression is considerably more of a problem in urban locations than in rural ones.

Would you care to comment on that?

Mr. **Loundy**. I think Mr. Stevens should.

Mr. **Stevens**. Well, Senator, it might be—I believe it was my testimony that started this, and there is a new retail deposit survey done by the American Bankers Association, which we believe is a rigorous effort to do this, and that is the basis for these conclusions that we have drawn about free checking is available at 80 percent of the banks to senior citizens, et cetera.

Senator **Metzenbaum**. Who did that study?

Mr. **Stevens**. The ABA had it done.

Senator **Metzenbaum**. The ABA.

Mr. **Stevens**. Yes, indeed.

Senator **Metzenbaum**. Well, what I am saying to you is that I think you have to look at the picture with respect to the banks concentrated in urban areas, totally distinct from those that are in Waukegan or Wasseon or wherever the case may be. I think it is a totally different picture, and I think the GAO acknowledges that fact. I had hoped that the ABA would.

You mentioned one thing, Mr. Stevens, about the fact that something—I remember one phrase was, we would be willing to work with you. I think it was to Senator Dixon. I have been trying to get the ABA to work with me on this subject for a long time. Is the ABA willing to work now with this Senator and this committee for the purpose of trying to bring about a piece of legislation on this matter of check cashing and lifeline accounts that would not provide a financial burden to the banks but would provide a great advantage to many of those who now cannot get their checks cashed?

Mr. **Stevens**. Yes, indeed, Senator. The Association stands ready to do that. We recognize that not everybody is served yet, and that would certainly be a goal we would like to try to achieve on an equitable basis.

Senator **Metzenbaum**. Don't come in before tomorrow morning, but I would be glad to see you. [Laughter.]

I would be happy to start working with you on it. [Laughter.]

Mr. Kelly, as you mentioned, 2 years ago, the Congress cut back on a bank's liability for covering a bad check. It has been reduced from 6-1/2 years to 18 months. The government can only go back to the bank to cover a loss 18 months from the date the bank cashed the bad check. It will go into effect this October. Now as I recollect this provision, it got into the banking bill 2 years ago, in part because the bankers thought that my check cashing proposal might prevail. You got it into the law now, but the fact is, the check cashing proposal still is not a reality.

I have to ask you, Mr. Kelly, this question. You represent the national banks, minority-owned banks.

Mr. **Kelly**. That is correct.

Senator **Metzenbaum**. How can you who are speaking for minorities in this country, not recognize the special problems that the minorities have with respect to this particular problem and not be coming in and saying we want to have a bill, let's try to work out something? In the past, we offered to let banks charge $2 per check. It is too much. I don't want to provide $2 any more, because that isn't your cost. It is less than that. Thirty-three cents is one figure, and then a small amount with respect to the exposure, which I figure out based upon the GAO figures, maybe a half a dollar a check, something like that. I don't understand why the National Bankers, why the National Bankers Association, I think that is the name of your group, isn't here saying this is right for the people that we represent, and we would try to work with you to develop a piece of legislature rather than coming in and telling us all the problems you have and why we shouldn't.

Mr. **Kelly**. Senator, we certainly would work with you and come up with legislation, but the reason we are here is because we would like to see our banks continue to exist and to continue to serve the very people that you are talking about. We are already serving our minority constituents, as I noted in my presentation, that most of our customers have accounts of less than $1,000 in their account. So we are already there serving them, but for it to be legislated that 75 percent or more of our deposit base, we won't have any control on the pricing of it, and also to thrust on top of that the cashing of government checks, without addressing the return and the accountability, you are talking about basically putting us out of business.

Senator **Metzenbaum**. Well, Mr. Kelly, let me say this. I was a banker. I was one of the principal holders, they were two of us, of one of the major national banks in Cleveland. I was on the board of another bank as well, at an earlier point. I understand enough about the banking business that I don't want to sit here and just say you ought to carry a burden, that you have to be an eleemosynary institution. I am not that stupid, but the fact is, I have been trying to get the banks to work with us on a piece of legislation for years, and I say to you that the minority bankers ought to be the ones specifically in the forefront urging these other people to come forward with a proposal so that we can work it out. I am disappointed that the minority bankers are here as part of this same resistance effort.

I don't want you to subsidize anybody, but I think you ought to just see to it that people have an opportunity to cash their checks and not be ripped off, as they are—not in all, but in some, check cashing places.

Mr. Chairman, my time is more expired.

Senator **Dixon**. Well, I thank the gentleman from Ohio, and I want everyone on this panel to know how useful their testimony has been and how helpful it is, and I assure every member of the panel representing all the different points of view and the economic interests represented here, that we will make an extremely careful evaluation of all of this before we arrive at any decision. There will be another hearing tomorrow. There will be a representative of the Fed here, and also in two separate panels representative groups again to address this same subject matter, and I assure you that all of this will receive our very careful evaluation, and that there will be discussions with the representative groups who are concerned about what we are doing.

Thank you all very much. This meeting is adjourned.

[Whereupon, at 11:50 a.m., the hearing was adjourned.]

GOVERNMENT CHECK CASHING, "LIFELINE" CHECKING, AND THE COMMUNITY REINVESTMENT ACT

WEDNESDAY, JUNE 7, 1989

U.S. Senate,
Committee on Banking, Housing, and Urban Affairs,
Subcommittee on Consumer and Regulatory Affairs,
Washington, DC.

The subcommittee met at 9 a.m., in room SD-538, Dirksen Senate Office Building, Senator Alan J. Dixon (chairman of the subcommittee) presiding.

Present: Dixon, Riegle, D'Amato, and Bond.

OPENING STATEMENT OF SENATOR DIXON

Senator Dixon. Ladies and gentlemen, today is our second day of hearings on several consumer issues which Senator Metzenbaum has sponsored. Once again, we have quite a number of witnesses to hear from so I'll make just a few opening remarks.

Today, we will hear about another controversial subject, the Community Reinvestment Act. It has caused much grief in some circles and done much good in others. I do not believe that the CRA has lived up to its potential. I think it should.

We will hear today about several success stories, certain instances in two great cities where CRA has worked. I hope we can learn from these examples.

Still, there are too many examples of the contrary. Generally, 98 percent of banks and thrifts get rated as a 1 or 2 on CRA. It seems incredible that 98 percent truly deserve top ratings.

I ask: For CRA to live up to its potential, need we change the law or only its enforcement? Would continuing oversight by Congress yield the best results or do we need to amend the Community Reinvestment Act itself? Will public disclosure improve CRA compliance or will it endanger efforts at stronger enforcement?

Second, banks and thrifts are not the only lenders in our communities. Increasingly, other lenders who are not covered by CRA are competing successfully. Are they meeting the credit needs of the whole community? Do they have a competitive advantage which in time could undermine CRA?

I do not have preconceptions about the answers to these questions, but I hope that the witnesses today will enlighten us and will engage each other. CRA works when each side lets go of its prejudices and grasps hold of new opportunities. Let us try to follow that example today.

Ladies and gentlemen, we're going to have two panels, but prior to those two panels we will hear from Governor Martha R. Seger of the Federal Reserve Board. We appreciate the fact that she will be here in a timely fashion and invite her to take the witness chair.

Governor Seger, we ordinarily limit the remarks to about 7 minutes, if that's satisfactory with you. I just want you to know that I appreciate your being here this morning and I will tell our mutual friend, Commissioner Bill Harris, that I was with you. Incidentally, Bill and I served in the Illinois House and Senate together through most of my General Assembly career and we were legislative leaders on opposite sides of the aisle through a good portion of that time. So he is a wonderful man and I will pass along to him your warm regards.

STATEMENT OF MARTHA R. SEGER, MEMBER, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM.

Ms. Seger. Thank you very much. I met your former colleague when I was banking commissioner in Michigan and he of course was and still is banking commissioner of Illinois, so that's how I know him and he's a fine fellow.

I thank you very much for inviting me here today and I particularly appreciate being able to come on early to accommodate my travel plans.

Also, I appreciate the opportunity to present the views of the Federal Reserve Board on proposals to amend the Community Reinvestment Act.

As I'm sure you know from our recent actions, the Board shares the subcommittee's interest in this important area. Also, I know the subcommittee heard testimony yesterday on basic banking and government check cashing and I would like to touch very briefly on those areas as well.

Senator Dixon. Good.

Ms. Seger. In regard to CRA, let me say at the outset that the Board believes that the purpose of CRA can best be accomplished when the process is, to the extent appropriate, open to public view and input.

Depository institutions are now required to prepare, annually update, and make available for public review, a CRA statement listing the exact loan products that they are willing to offer.

We recently joined the other financial regulators in issuing a joint CRA policy statement which encourages institutions to better inform the public regarding their CRA activities. The policy statement shows our commitment to widening the channels of communication among banks, communities and regulators and underscores the idea that people who are well informed about the activities of their local financial institutions are better equipped to participate in the CRA process.

Our new policy statement urges institutions to significantly expand their CRA statements to paint a more complete picture of their overall approach to CRA. For example, the expanded statement would describe strategies for marketing and advertising, credit needs assessment, and new product development, as well as past accomplishments and future plans to meet community credit needs.

The agencies believe this additional communication can be achieved without imposing significant burdens on the industry. Banks should be able to tell their communities what they are doing to help meet credit needs without incurring much, if any, additional cost since they should be evaluating their CRA statements on an annual basis anyway.

If institutions take this opportunity to share their achievements with the community, we think solutions to CRA can be accomplished outside the tension of the application process.

We also believe that this enhanced communication should take place in a way that does not make the regulatory process for CRA more complicated or costly or impose delays on those institutions with good records of CRA performance.

Over the last 10 years the Federal Reserve has established a three-faceted program to carry out our mandate under the CRA. The program includes CRA examination by specially trained examiners approximately every 18 months for most State-member banks, community affairs officers at each Reserve Bank, and consideration of the CRA record of banks in connection with applications received under the Bank Holding Company and Bank Merger Acts.

A major thrust of the CRA policy statement is to shift the CRA emphasis away from the applications process and to build stronger enduring mechanisms for outreach and service by institutions to their communities on an ongoing basis.

The CRA revisions in S. 909 would require that the numerical ratings and a written assessment of an institution's CRA performance be made available to the public. We continue to support public disclosure of an assessment of each institution's CRA record of performance, as we did in our testimony last September.

Let me emphasize that the written evaluation we support should be a summary of the examiners' conclusions and support for them, but not the same as the examination report itself.

Because of our opposition to credit allocation, we do not support requiring the evaluation to place special emphasis on low and moderate income housing, small business, and small farm loans. We are strongly opposed to public disclosure of CRA ratings themselves which, like commercial bank examination ratings, have been treated with strict confidentiality by all the regulators.

We believe disclosure of these ratings may interfere with the communication between the bank and the examiner that is essential to the supervisory process. These ratings may also be misleading and may detract from the narrative analysis.

Other revisions to the CRA proposed in amendments to H.R. 176 late last year comprise a broad spectrum of measures pertaining to CRA examinations, assessment factors for CRA performance, and a treatment of CRA issues in the application process.

While we believe that public disclosure of CRA assessments has merit, as discussed earlier, we have strong reservations regarding many of the proposed amendments that would, in our view, unnecessarily encumber existing administrative procedures for CRA enforcement.

Now I would like to briefly address the government check cashing and basic banking bills that have been introduced in the Senate.

To begin, let me say that the Board shares the belief underlying these bills that banking services should be widely available to all who choose to use them. To underscore this, several years ago we joined with the other financial regulatory agencies in issuing a policy statement on basic financial services. It encouraged institutions to recognize and meet the needs of consumers for safe places to keep funds, for ways to obtain cash, and for ways to make payments to third parties.

I know that it has been suggested that low-income persons are being priced out of the market for banking services by increases in fees and charges. We have spent some time studying account ownership patterns by various segments of the population and have not seen any significant decline between 1977 and 1986.

Therefore, we are not persuaded that increased costs have driven people out of the system. There are many reasons why people may choose not to have a bank account, including convenience, difficulties in managing an account, and general distrust of banks.

Also, let me note that while various surveys have reached different conclusions, there is evidence that suggests that financial institutions are making check cashing services and basic banking accounts available to people who choose to use them.

While we understand the concerns that have been raised, and in the policy statement have encouraged financial institutions to address them, we are not convinced that a problem warranting legislation has been demonstrated.

We believe that significant results have been achieved through the voluntary efforts of financial institutions and that this approach is preferable.

We have some specific concerns with these bills and I have detailed them in my written testimony. Basically, we do not think it is wise for government to require institutions to offer specified banking services at set prices. We are also concerned about the increased potential for fraud that could result from this bill Also, mandating one basic banking product could result in a standardization of account offerings and reduce the likelihood that institutions will offer products tailored to the particular needs of their customers.

Finally, we believe that direct deposit should be encouraged and that alternatives such as electronic delivery of government benefits should be explored.

Thank you very much for giving me the opportunity to present our views.

[The complete prepared statement of Ms. Seger follows:]

For release on delivery
9:00 a.m., E.D.T.
June 7, 1989

Statement by

Martha R. Seger

Member, Board of Governors of the Federal Reserve System

before the

Subcommittee on Consumer and Regulatory Affairs

of the

Committee on Banking, Housing, and Urban Affairs

of the

U. S. Senate

June 7, 1989

SUMMARY

The Board believes that the purpose of CRA can best be accomplished when the process is, to the extent possible, open to public view and input. Recent action by the financial regulators in issuing the CRA Policy Statement, which encourages institutions to better inform the public regarding CRA activities, underscores the idea that people well-informed about the activities of their local financial institutions are better equipped to participate in the CRA process. We continue to be committed to widening the channels of communication among banks, communities and regulators, but believe this should be done without making the regulatory process for CRA more complicated or costly, or imposing delays on those institutions with good records of performance.

Over the last ten years the Federal Reserve has established a three-faceted program to carry out our mandate under the CRA. The program includes CRA examinations by specially trained examiners approximately every 18 months for most state member banks, Community Affairs Officers at each Reserve Bank, and consideration of the CRA record of banks in connection with applications received under the Bank Holding Company and Bank Merger Acts. A major thrust of the CRA Policy Statement adopted by the federal financial supervisory agencies is to shift the CRA emphasis away from the applications process and to build stronger, enduring mechanisms for outreach and service by institutions to their communities on an ongoing basis.

The CRA revisions in S. 909 would require that the numerical ratings and a written assessment of an institution's CRA performance be made available to the public. We support the concept of public disclosure of an assessment of each institution's CRA record of performance as we did in our testimony last September. We would like to emphasize that the written evaluation should be a summary of the examiner's conclusions and support for them, but not the same as the examination report itself. Because of our concern regarding credit allocation, we do not support the concept that the evaluation should place special emphasis on low- and moderate-income housing, small business and small farms loans. Additionally, we are strongly opposed to public disclosure of CRA ratings which, like commercial bank examination ratings, have been treated with strict confidentiality by all the regulators.

Other revisions to the CRA considered late last year comprise a broad spectrum of measures pertaining to CRA examinations, assessment factors for CRA performance, and the treatment of CRA issues in the application process. While we believe that public consideration of the CRA assessment has merit as discussed earlier, we have strong reservations regarding many of the provisions in this proposal that would, in our view, unnecessarily encumber existing administrative procedures for CRA enforcement.

With regard to the government check cashing and basic banking bills, the Board shares the belief that banking services should be widely available and has issued a policy statement to this effect. However, the Board has sponsored surveys that do not appear to reveal a significant decline in account ownership over the years. In addition, while various surveys have reached different conclusions, there is evidence that suggests that check cashing services and basic banking accounts are being made available. Accordingly, it is not clear that a problem that would warrant such legislation is present at this time.

The Board has other concerns with these bills. First, the Board does not believe it is wise for government to require that specific banking services be offered and to set the price for such services. We are also concerned by the potential for fraud that would exist if the check cashing bill is enacted. In addition, the basic banking bill could result in a standardization of account offerings and reduce the likelihood that institutions will offer products that are tailored to the particular needs of their customers. Finally, we believe that alternatives such as electronic delivery of government benefits should be explored instead.

* * * * *

STATEMENT

Thank you for the opportunity to provide the views of the Board of Governors of the Federal Reserve System on legislation relating to the Community Reinvestment Act (CRA), the Government Check Cashing Act of 1989, and the Basic Banking Services Access Act of 1989.

The CRA revisions in S. 909 would require that the numerical ratings and a written assessment of an institution's CRA performance be made available to the public. In addition, S. 906 would require depository institutions to cash government checks at cost for non-customers provided that such persons have registered with the institution. S. 907 adds the requirement that depository institutions offer, for minimal fees, "basic financial services accounts" that have low minimum balance requirements and permit at least 10 withdrawals per month.

Community Reinvestment Act

To preface our discussion of the legislation pertaining to the CRA, I'd like to underscore our belief that the purpose of the CRA can best be accomplished in an arena which is, as much as possible, open to public view and input. Recent actions by the Board in concert with other regulators have echoed a theme that seems to be at the heart of the proposals before you today -- that people well-informed about the activities of their local financial institutions are better equipped to participate effectively in the CRA process. We are also committed to widening the channels of communication among banks, their

communities and regulators, but we believe this should be done without making the regulatory mechanisms and procedures for the CRA more complicated, costly, or apt to impose delays on those institutions with good records of performance.

I'll begin by describing briefly the three-faceted program we've established to carry out our mandate in enforcing the CRA. First, the Federal Reserve's specialized consumer compliance examiners conduct examinations of CRA performance about every eighteen months for most state member banks, and more often for those with identified weaknesses in their record. The examination takes a comprehensive look at the bank's activities to address credit needs in its market, including those of low- and moderate-income areas, as well as the kinds of relationships it is forging with specific segments of the community. Second, through the community affairs office at each of the Reserve Banks, we provide information about community development strategies and techniques to banks, bank holding companies, and others. One of our primary goals is to become familiar with the credit needs within the Federal Reserve districts, and then help banks construct programs which respond to those needs. Third, we consider the CRA record of banks in connection with applications received under the Bank Holding Company and Bank Merger Acts; CRA performance is taken into account along with legal, financial, managerial and competitive factors.

Our commitment to enhancing the role the public plays in the CRA process has been a long-standing one. For more than ten years, we have endeavored to ensure that CRA examinations are not conducted in a regulatory vacuum -- Federal Reserve examiners routinely interview businesspeople, government officials, housing and other community group leaders in the bank's community to learn about the local economic environment and the perceptions these individuals hold of their local financial institutions. We require institutions to keep a file of letters commenting on their CRA performance from members of the community; examiners review those letters, as well as the institutions' responses to them. Careful attention is also given to public comments on CRA performance, or protests, received in connection with an application. Yet our experience with the CRA leads us to believe that more can be done to open up the process -- and that is precisely the direction in which we are moving.

In March of this year the Board, together with the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board adopted a CRA Policy Statement to provide guidance to institutions and to community groups, and to clarify a number of issues which have arisen in enforcing the CRA. For example, institutions are presently required by regulation to prepare, annually update, and make available for public review a CRA Statement listing the loan products they are willing to extend. The new policy statement urges each institution to significantly expand its Statement to paint a picture of the institution's overall approach to CRA, describing strategies for marketing and advertising, credit needs

assessment and new product development, past accomplishments and future plans. Naturally, the size, resources and location of an institution will influence the CRA Statement's degree of detail and its scope. While an expanded statement laying out the details of its CRA efforts may be extremely useful to a large bank in a major city, it may simply not be necessary for a small bank in a rural setting to go into similar detail.

A major thrust of the policy statement is to shift the "CRA spotlight" away from the applications process -- with the pressures imposed by our timetable guidelines for completing the process -- and to build stronger, enduring mechanisms for outreach and service by institutions to their communities. We think the expanded CRA Statement is an ideal vehicle for doing that by focusing the attention of an institution's management, and of the public at large, on the institution's record on an ongoing basis, and on any areas needing improvement. At the same time, we have strongly encouraged community organizations to take advantage of the expanded CRA statements as a starting point for discussion, bringing their concerns to the attention of an institution's management -- to the greatest possible extent -- in the framework of a continuing dialogue, rather than in a protest situation.

A second important policy direction emphasized in the new policy statement should be borne in mind in considering proposed legislation. That is, that institutions desiring to expand their operations should have appropriate CRA policies in place, and working well, before filing an application. That means that while commitments by applicants for future actions may be used to address specific problems in an otherwise satisfactory record, making commitments to improve in the future should not be seen by applicants as a way to compensate for a seriously deficient past record of performance.

This approach was demonstrated earlier this year in the Board's denial of an application by Continental Illinois Bancorp, Inc., of Chicago, Illinois, to acquire an Arizona bank. In its order, the Board described, and took a positive view of, a plan developed by Continental to correct shortcomings in its CRA performance, which was in initial stages of implementation. Yet the prior record failed to demonstrate, in the words of the Board's order, "a basic level of compliance on which the commitments can be evaluated." The Board's handling of the Continental case should not be interpreted as evidence of any lessened willingness to work with institutions directly, or through their primary regulators, to improve their record. While there were reasons for the Board's denial in addition to CRA factors, the case does give a clear signal that, with respect to the CRA, institutions should "put their houses in order" before considering expansion. It also highlights the importance of an established record of performance under the CRA.

S. 909

In light of these developments, let me now turn our attention to S. 909, which would amend the Community Reinvestment

Act to require the regulatory agencies to prepare written evaluations of institutions' performance under the Act, and to make those evaluations public. We support the concept at the core of Senator Metzenbaum's proposal; in fact, you may recall that Governor Johnson endorsed the idea of regularly publishing an assessment of each institution's CRA record by our examiners in testimony before this Committee last September.

But one point is especially worthy of emphasis with regard to the nature of the written evaluations for public release that we support. Though the public evaluations we support would summarize the examiner's conclusions, together with supporting information related to the CRA assessment factors, these evaluations would not be the same as the examination reports themselves. Neither would they divulge material contained in the examination report which is important for supervisory purposes, but must be treated confidentially -- such as information about the financial condition of the institution, and any sensitive information about its employees, customers or members of the community. We believe the relevant provisions of S. 909 should be written to recognize the distinction between the examination report that is given to the bank and the summary assessment that we believe can usefully be made public.

The objective of that proposal was to tell people at the community level in a concise, straightforward and timely way how well their local institutions are doing under the CRA. Doing so should facilitate exactly what we are endeavoring to do through the Policy Statement just described -- promote the early start of a constructive dialogue about CRA achievements and goals. Those concerned about affordable housing, minority businesses, inner city reinvestment and many other areas will have the benefit of knowing how these factors have been weighed in assessing the record, and what areas for improvement have been identified.

We do, however, have serious concerns about two aspects of the proposal. First, the written evaluations of each institution's performance would be required to emphasize three specific types of credit -- loans for low- and moderate-income housing, small business and small farms. We believe this is inconsistent with the intent of the Act itself, which does not impose any specific lending requirements. Rather, institutions have a responsibility to help meet local credit needs utilizing their own expertise and resources.

Because needs vary widely from community to community, we would be remiss in rigidly focusing on these three credit categories in making our evaluations. CRA examiners aim to take a broad picture, instead of a snapshot, of all activities by an institution that foster community revitalization -- principally direct loans of all kinds, but also, for instance, participation in the secondary market, purchase of state or municipal bonds, and investment in or technical assistance to community development projects. Examiners do look at the amounts and distribution of credit extended for housing, small business and

small farms, not with the intent of making a quantitative analysis of an institution's lending, but in order to gain a full, balanced view of its service to the community.

Secondly, the bill would mandate public disclosure of the numeric ratings assigned during examinations. Historically, CRA ratings, like commercial examination ratings, have been treated with strict confidentiality, as required by procedures adhered to by all regulators. The ratings were designed as a kind of supervisory shorthand to help us monitor those institutions needing closer attention; the numeric rating is in no way a self-explanatory indicator of performance. Moreover, a rating assigned at a particular date in the past can be misleading, given that CRA performance should be seen as a process developing over time, rather than a static state of affairs. At the very least, release of the rating number would divert attention from the substance of examination findings. Of even greater concern is the potential for the undermining of public confidence in the safety of deposits in an institution, if an adverse CRA rating were to be misunderstood as a reflection on its financial soundness. Much more can be achieved by making public only the narrative evaluation, as suggested by Governor Johnson last September.

CRA Amendment to H.R. 176

Your letter asked that we address other CRA changes proposed in an amendment to H.R. 176 late last year. This proposal comprises a broad spectrum of measures pertaining to CRA examinations, assessment factors for CRA performance, and the treatment of CRA issues in the applications process. Here again, we believe the aspect of the proposal dealing with a public CRA assessment has merit. Our overriding concern, however, is that many of its provisions unnecessarily encumber existing administrative procedures for CRA enforcement.

First the bill requires in Section 804(b) that the agencies give public notice prior to commencing CRA examinations. Presumably this would be done through newspaper advertisements, since it must be given "in a manner reasonably designed to reach members of the community served by the institution under examination" -- although the use of lobby notices in the institution, or publications currently disseminated by each Reserve Bank which list pending applications might also be envisioned.

To gauge the implications of this proposal, Reserve Banks surveyed local newspapers to estimate the costs involved in running the 26,500 notices which we estimate would be required every two years for the examinations by all the federal regulators, assuming every institution is examined at least every two years. The total bill would be on the order of $1.24 million biannually, taking into account price differences in urban and rural areas. Time involved in identifying suitable newspapers and making publication arrangements could add considerably to the price tag.

As stated in the proposed statutory language, the reason for the provision is to allow any person to submit comments on an institution's record in connection with CRA examinations. Actually, this has long been our practice. In the Federal Financial Institutions Examination Council's A Citizen's Guide to CRA, for example, community members are encouraged to discuss their concerns with the institution's regulatory authority, particularly through the public file, the maintenance of which is one of the CRA's statutory requirements. As indicated in the Guide, persons who request to speak to a Federal Reserve examiner in letters to the public file will be contacted during the next scheduled examination.

In reality, we go far beyond this provision, in that we welcome comments about any institution's performance at any time, not just in connection with examinations, and we take them very seriously. We also seek out public input each time we conduct a CRA examination through the community contact interviews I mentioned earlier. In 1988, Federal Reserve examiners alone interviewed some 925 consumer advocacy groups, housing coalitions, local business and trade associations, as well as local government officials, and factored their comments into their assessments of CRA performance. Given the totality of these efforts, we do not believe this additional expense for soliciting public comments in the examination process is necessary.

The bill's Section 804(e) calls upon the agencies to prepare and make public its assessment of each institution's performance under the CRA. This concept has our support, for the reasons already discussed in connection with Senator Metzenbaum's proposal. There is, however, a need to clarify that the assessment would be separate and distinct from the examination report and the numeric rating.

Provisions of the bill's Section 805 regarding the consideration of CRA performance in the application process are troubling to us. We note that it would require the agencies to rely on the "most recent assessment of such record" in considering an applicant institution's performance. Experience has shown us that the most recent assessment may not always be the only, or most reliable, indicator of current performance, especially when the examination report is outdated, or when an institution has undergone a major internal change, such as turnover in management. In such instances, the flexibility to look beyond the latest examination report for up-to-date information accurately reflecting present performance is essential.

Section 805(e) sets out timing requirements for agencies to complete their assessments of CRA records in the framework of applications that we think are unnecessary and unwise. You may be aware that under Regulation Y, the Board has imposed on itself a 60-day guideline for processing applications. The vast majority of domestic bank and bank holding company applications

are processed well within the 60-day goal; in both 1987 and 1988, the average processing time for over 4,000 domestic cases, including those with CRA issues, was 39 days.

Under the Board's Rules of Procedure, the presence of a CRA protest or an adverse assessment by any agency makes the case a matter for Board attention -- though it may be returned to the Reserve Bank after Board staff review. It also can make the process more complex, requiring a thorough, and frequently time-consuming, analysis of the issues. In many instances, it is necessary for us to seek out additional information from the applicant, or its primary regulator, to fully address these issues. This is why we are not always able to meet the 60-day target, although delays have generally not been inordinate; in 1987, average processing time for the 37 CRA-protested cases was 73 days and in 1988, for 32 cases, it was 87 days.

At the outset, we would question whether imposing statutory timeframes on applications processing would achieve the desired end. They would seem to hamper, rather than help, our efforts to give appropriate attention to convenience and needs considerations in applications, especially where an applicant's performance has been marginal, or where the applicant is not readily able to provide detailed information about its record.

Apart from our general concern about these requirements of the bill, other aspects of the bill's timing provisions are unclear. CRA is only one of many issues considered as part of these applications. The Board also considers legal, financial, managerial, and competitive issues, as well. The draft seems to speak only of those cases where CRA issues are brought forward through a protest. In fact, CRA issues may also be uncovered by Federal Reserve Bank or Board review, when any of the banks party to an application have been assigned adverse CRA examination ratings by any of the agencies' examiners. In addition, the draft appears to require that the CRA assessment in an application be completed by a certain time in the application process, whether or not the analysis of any other issues the case might raise have been completed and the overall case is ready for final decision.

Let me mention briefly our policy regarding extensions of the comment period since misperceptions about our policy may have sparked interest in the statutory timeframes. We believe it is incumbent on persons desiring to comment on an applicant's CRA record to do so within a 30-day period; otherwise, we may be unable to give their comments the attention they deserve, and still carry out our responsibility to process applications in a timely manner. In a very few circumstances we do find an extension of the comment period is warranted -- where the application has not been promptly made available for inspection by the parties, for example, or in the rare event there has been inadequate public notice of the application. But we do not think it is appropriate to extend the comment period -- and possibly delay the Board's decision on the case -- simply because the commenter wants more time to pursue negotiations with an institution under the pressure of a pending application. The agencies' recent Policy Statement stresses this point.

In summary, the amendment to H.R. 176, in our view, poses a number of problems. Most importantly, it would make more rigid and cumbersome procedures which for the most part are already in place for enforcing the CRA, without presenting any really new approaches to make the process work better. We stand ready to answer any questions you may have, and to continue working with the Committee in this key policy area.

Check Cashing and Basic Banking

Let me turn now to the government check cashing and basic banking bills that are under consideration. These result from concerns that are similar to those that motivate the Community Reinvestment Act. Not only are some questioning whether banks are meeting the credit needs of their communities, but concerns have also been raised that low- and moderate-income persons may not have ready access to banking services. In particular, the focus has been on the need to cash government checks and to have an account for making a limited number of payments to third parties.

The Board is quite familiar with these concerns. Since 1977, we have sponsored four surveys that determined, among other things, the number of families that do not have depository accounts. While the General Accounting Office has reported a higher number, our research suggests that the overall percentage of families without accounts has remained fairly constant at about 8-12% between 1977 and 1986. This research has also indicated that roughly 30% of the families whose income falls in the lowest quintile do not hold accounts. Although the percentages for this latter group have fluctuated, the numbers were more or less the same in 1986 as in 1977. Thus, while many low-income families do not have accounts, the fact that the percentage has remained relatively constant suggests that the increase in fees and minimum balance requirements in recent years has not caused a significant decline in account holding. There are probably more fundamental reasons for much of the lack of account ownership. For example, the convenience of check cashing alternatives, the fact that these families may have few bills to pay, and the difficulties in managing an account with limited resources may explain, to a large degree, why some low-income families do not have an account relationship. Also, it may be some people simply do not trust banks and prefer not to deal with them.

Nevertheless, we share the belief that banking services should be widely available to all. Several years ago, the Board adopted a Joint Policy Statement on Basic Financial Services with the other federal financial regulatory agencies and with the state financial institution regulatory associations. The Policy Statement encouraged financial institutions to recognize the need of consumers for a safe and accessible place to keep money, the need to obtain cash (including cashing government checks), and the need to make payments to third parties. The Policy Statement

encouraged institutions to continue to develop account products that are responsive to these needs.

In the Policy Statement, the Board supported a voluntary rather than a mandated approach so that institutions could have flexibility in developing account products that meet the particular needs of their customers. That remains our preference, and we oppose legislation to require institutions to offer specific banking services.

First, it is not clear that these services are so widely unavailable at present that legislation is warranted. Over the last several years, a number of surveys have been conducted to assess the availability of basic banking and check cashing services. While results vary, there is evidence that a widespread problem does not exist. For example, in its recent report to Congress on government check cashing, the GAO reported that, as of 1985, 86% of banks and 55% of thrifts cashed U.S. Treasury checks for non-customers. The American Bankers Association reports that over half of all banks, and over 70% of large banks, offer basic banking accounts and that the number of institutions offering such accounts has increased dramatically over the years. Following a survey of virtually all financial institutions in New York state, the New York State Banking Department found that low-cost banking services are widely available and that the vast majority of low- and moderate-income persons have ready access to such accounts. In a 1987 report, the GAO found that a 74% of financial institutions provide low-cost accounts to senior citizens.

These surveys suggest that check cashing services are often available to non-customers who choose to use them and that a substantial and increasing number of financial institutions voluntarily offer basic banking accounts. Consequently, the Board does not believe that enough of a problem has been demonstrated to justify sweeping legislation.

The Board has a number of other concerns with this legislation. First, as a general matter, we question whether it is wise for the government to mandate the services that financial institutions must provide. This is particularly so when the legislation involves setting the fees for such services. If there are problems in the way government funds are delivered to recipients, then it seems that the government should itself assume more responsibility for addressing the difficulty. For example, it might be useful to explore the possibility of using federal post offices to provide check cashing services to holders of government checks since they offer other financial services such as money orders. Electronic delivery of government benefits is another avenue that could be vigorously pursued. Successful electronic benefits delivery systems are currently operating, including programs in New York City and St. Paul, Minnesota. The advantages of these systems -- for beneficiaries, government agencies, and financial institutions -- are numerous. They include eliminating problems with delayed, lost, or stolen

checks, providing quicker resolution of problems concerning payments and lowering costs to all parties.

A more specific concern involves the mechanism for setting fees for the services. The bills require the Board to study financial institutions' "actual" costs and to set the fees permitted to be charged for these services to recover these costs. In addition to the many difficulties of trying to determine such costs, any fees set by the Board would almost certainly be an average and, as such, could never reflect the actual differences among institutions. As a result of a federally-established fee, some institutions would fail to recover their costs, while other institutions could exceed them under the national fee standard. Finally, it appears inequitable that financial institutions would be required to offer these services at cost while other entities, such as check cashers, could continue to offer them at a profit.

The Board is also concerned that financial institutions would increasingly fall victim to fraud if check cashing legislation is enacted. Checks can easily be stolen, and identification cards can easily be forged. Giving the Board the authority to suspend the check cashing requirement for certain classes of checks, as the bill does, is small comfort. It would take a relatively long period of time for the Board to learn of any patterns of fraud and, by then, significant losses may already have been suffered. Also, while fraud levels may now be low for U.S. government checks, this may not continue to be the case following legislation. Institutions can now keep fraud losses low by establishing procedures, based on their own experiences, that are adequate to address their own risks. Mandatory standards may eliminate their ability to continue using methods that have been successful for them and may leave them far more vulnerable.

The Joint Policy Statement I mentioned had the benefit of putting the Federal government behind providing basic services, while leaving the implementation to the creativity of individual institutions. Conversely, a single federally-mandated banking service may stifle innovation and experimentation. A number of different account products have evolved as a result of voluntary efforts by financial institutions. Some, for example, involve savings accounts with money orders used for third-party payments. Others, based on a "pay-as-you-go" idea, have fees for each check, rather than the monthly maintenance fee contemplated by the legislation. Either of these could be better and more economical for the person who writes fewer than 10 checks a month. The basic banking bill will likely result in the standardization of accounts, and it runs the risk of thwarting the continued development of different services, such as these, to address varying and changing needs of low income and elderly individuals. Institutions may have much less incentive to offer additional, and potentially cheaper, basic banking accounts once they offer the standard service required by law.

Other innovative arrangements are being investigated that would eliminate many of the problems with delivering government benefits by paper checks. The Board strongly supports the facilitation of electronic alternatives for the delivery of government payments (known as "electronic benefits transfer" or EBT). These arrangements are probably a better long term solution to the problems that motivate the check-cashing legislation.

Since the Board testified on similar legislation last fall, interest in electronic benefits transfer has increased. A number of meetings have been held among representatives of government agencies, financial institutions and consumer groups to discuss the feasibility of such arrangements. In addition, several programs are now operating and others are about to be initiated. The Board agrees with the GAO's conclusion that electronic delivery provides several advantages over a paper-based government benefits system. Consequently, we are very encouraged about the increased momentum in EBT activity over the last several months. We urge the Congress to foster these efforts, rather than imposing burdensome new requirements on financial institutions.

Finally, in our experience, well-intentioned legislation and regulations, particularly as they pyramid on one another, can cumulatively be overwhelming -- especially for small institutions. This bears particular note when it is not clear that a compelling need for the legislation has been demonstrated.

The Board believes that voluntary efforts by financial institutions will continue to be successful in meeting many of the concerns that have been expressed without the burden and cost that rules and regulations inevitably impose. Alternatives such as EBT, in particular, merit future exploration. For all the foregoing reasons, the Board opposes the basic banking and check cashing bills now being considered by the Senate.

Senator **Dixon**. Governor Seger, I appreciate that very much. I believe, if you don't mind, I'm going to stick pretty close to the CRA questions because we had such a long hearing on the government check cashing and lifeline checking questions yesterday.

First of all, I would appreciate it if you would have staff send to my staff here in the committee the things that you support in this bill on the CRA question and your reasons why that will work OK, and the things you oppose in it and the reasons why you at the Fed think that's a bad idea.

Now in a simplistic way, because of course you have more expertise in the field than I do, I would like to understand why you don't mind giving them a sort of a résumé or something of that sort—I think you said not the original itself but some kind of a résumé of your findings on a CRA question with reference to an institution—but you don't want to give them numerical ratings.

Now I have to tell you that as a person who has no expertise in the field I don't understand that. Why would you make that distinction?

Ms. **Seger**. The best way I can explain it is to use a teaching analogy. I taught in college for 5 years and I will tell you that it's very difficult to get down to the specifics of a grade. And honest teachers will tell you that when they give somebody an A− rather than a B+, there's a lot of subjective judgment involved. If taken to the mat, it would be very difficult for me when I was teaching to defend giving somebody the B+ rather than the A−.

And the same I think is true here. You can make general determinations of the top performers and the worst performers and then some big glob in between, that is possible to do, and that's what the written appraisal would basically do. It would verbalize how well the organization is doing.

THE RATING SYSTEM

Senator **Dixon**. If I may interrupt, you are saying that the Fed in your view should make available some kind of an evaluation in writing that is a summarization of what the findings have been with reference to the Continental or the First in Chicago, without saying this is a No. 1 or this is a No. 2.

Ms. **Seger**. Right.

Senator **Dixon**. How many numbers are there?

Ms. **Seger**. Five.

Senator **Dixon**. You can be anywhere from 1, which is the best, to 5, which is the worst.

Ms. **Seger**. Right.

Senator **Dixon**. With the assertion being 98 percent that are already ranked 1 and 2, I would almost argue that if 90 percent are ranked 1 and 2, it doesn't hurt much to put the numbers out because anybody who's 1 or 2 can make a case they're not doing too badly; and if you're 3, 4 or 5, you must be doing awfully badly if more than 90 percent are 1 or 2. Could I make that observation and ask what you think?

Ms. **Seger**. Well, I think those institutions that are rated 2, would probably be upset and would see, by the way, what we've given their competitors. They would say, "Well, I think I'm as good as this bank across the street and you gave them a 1 and you only gave me a 2."

Senator DIXON. Let me ask you this, Governor. As in any legislative process, there are those who feel very strongly on one side and those on the other. I would like to accommodate the points of view to get a bill here and we are seeking that kind of common ground.

For instance, on check cashing we talked about the fact that banks and thrifts are not eleemosynary institutions, financial institutions. They've got to make a profit and we've got to protect them against fraud and other things because they are not charitable institutions. They are in business to make a profit.

I hope you understand that that applies to this as well. For instance, I was at the First National—one of their representatives is in the audience—a couple of months ago and Gale Cincotta and that group from out there that has done this marvelous work in the neighborhoods were there. I expect Gale forced them to do more than they wanted to do in the first place, if candor is required in these discussions, but the point is that they've done a great deal and hundreds of millions of dollars have gone out into the community and done this fabulous work, and the good side is that banks made money too. Everybody is happy.

So those are the kinds of things we like to see occur.

Ms. SEGER. You just verbalized the performance. That's what we're saying should be done. You can put it in words rather than equate it to a 1 or a 2.

Senator DIXON. Here's my thinking on it. I wonder whether there would be a possibility of accommodating the sponsor of this bill and others—I'm not one of the sponsors—by finding a way that we could at least in the appraisal of what you have done indicate whether this institution has been satisfactorily performing, a finding of satisfactory performance, or we are disappointed in the Jones Bank of Bellville and it is not doing a satisfactory job. Could there be a finding of some kind of direct consequence in that regard? Would the Fed put its imprimatur on an institution and say that this institution is doing their job in CRA or, on the contrary, say they are not doing their job and the communities are not being served well? Something like that rather than the 1, 2, 3, 4, 5? Maybe keep the 1, 2, 3, 4, 5 for your internals, but do this? What do you think of that?

Ms. SEGER. Well, that's exactly what we had in mind, that we would, for example, say the bank you alluded to in Bellville, Illinois has a very strong CRA performance and then pick off the things that they have done that contribute to this very good rating.

Senator DIXON. Or you could say that such an institution has not done too well and we're disappointed they don't do more of this, this and this.

Ms. SEGER. Right. And that they have less than a satisfactory grade. But less than satisfactory could be in general terms without nailing down exactly which number might apply.

Senator DIXON. For the edification of this Senator, how do you do this? How do your examiners interview people in the community and find these things out? If you could make a note or two, how do you do it? What community groups do you talk to? When do you talk to them? For how long? What sort of information is gathered and recorded? Give me a picture of how you'd go into Chicago or Peoria or someplace and find out about community involvement.

Ms. **Seger**. Well, again, I suspect that going into Chicago is going to be different from my home town of Adrian, MI, because of size.

Senator **Dixon**. Or my home town of Bellville, which is 45,000.

HOW RATINGS ARE DETERMINED

Ms. **Seger**. OK. But we do try, in whatever size community, to select both some local government people—and representatives of community groups—and you have to be arbitrary. Again, in Chicago, we are not doing a scientific survey or a census and getting everybody, certainly, and we wouldn't claim that. Rather, we interview some economic development people, and some representatives of community groups such as Gale Cincotta. And we'll talk to government agencies there, folks in the city.

Senator **Dixon**. You might talk to the mayor in Bellville?

Ms. **Seger**. Sure, or an economic development agency in the city, if there is one, or church groups, a wide spectrum.

Senator **Dixon**. Real estate agents, would you talk to them?

Ms. **Seger**. Right. And community organizations such as New Detroit, along with the real estate agents. We would be trying to get some flavor from different kinds of people of how they view this particular institution's willingness to serve the community's credit needs. Because again, credit needs encompass more than just making loans to buy houses. Credit needs can also be served by business loans, education loans, whatever.

Senator **Dixon**. Well, Governor, I'm going to yield in a minute to my distinguished friend from Missouri, the ranking member here, Senator Bond, but let me just see in conclusion if I have the flavor of your testimony.

The essence of your testimony is that you think that this whole business of upgrading a way of understanding how involved the financial institutions are in the communities is not out of line, there's some value in some kind of a bill that upgrades that somehow; but you don't think that just putting a number 1, 2, 3, 4 or 5 on it is the criteria. That what we ought to do is have some kind of an analysis of what you folks at the Fed see that the banks have done in the community that is not the whole substance but a reasonable report by the Fed and that you would be willing to have an indication of how the Fed evaluates performance of the institution by sort of generic standards—it's better than average, it's not as good as average?

Ms. **Seger**. Right.

Senator **Dixon**. I think that's satisfactory from this Senator's standpoint and helps me a great deal.

The Senator from Missouri.

Senator **Bond**. Thank you very much, Mr. Chairman.

I apologize for being late. We had another meeting this morning and I had a chance to look over Governor Seger's testimony and I'm delighted to have a chance to ask her a couple of questions.

CRA CHALLENGES

Governor Seger, one of the issues that banking and consumer groups have disagreed over and will disagree on probably today is how long CRA challenges delay the approval of contested applications. Later this morning, there will be testimony based on Federal Reserve figures that CRA protests only delay applications for a couple of days.

Do you think this is accurate?

Ms. SEGER. Well, it's the difference between averages or extreme cases. On average, it's a few days. We give ourselves a 60-day target date for processing an application, and there are other things to look at, such as financial, managerial, and competitive issues, even on protested ones. If a protest comes up, much of that can be handled within this 60-day period that we have given ourselves to process these applications.

But there have been some of the more complicated applications, some of the very ugly protested ones, that have gone on longer than 100 days. These are the ones, particularly if it's your application that's been protested and has been held up for over 100 days, that people have in mind when they say that these protests have worked this way. I don't think that's typical, but it has happened in certain cases.

Senator BOND. OK. Why do you believe it's important to shift the emphasis in CRA enforcement away from the applications process toward more ongoing discussions between the regulators, community groups and the banks about how community needs can best be met?

Ms. SEGER. What we're trying to accomplish is to have the banks serve their communities in an ongoing way. I think that's the ultimate objective of CRA. The ultimate objective of CRA is not to just have the institution meet some particular bureaucratic set of requirements and have it posted in the lobby. That's part of it, but what you really want institutions to do is serve their communities. I don't think that you just want to take a snapshot or give them a test when they have an application coming in. I think we ought to encourage them to be good boys and girls consistently over a long period of time and then, if they have an application, then obviously they have a track record for us to look at.

But there are almost 14,000 banks out there and not all of them are merging and consolidating or acquiring other institutions, so I think we ought to be encouraging everybody along these lines.

So my view is more encompassing than placing the entire emphasis on the application.

Senator BOND. Well, that makes a lot of sense to me. I wanted to hear you explain it again and I'd like to ask your view as to whether you think banks can find these community involvement activities profitable. From what you've seen, can the banks who are fulfilling their CRA responsibilities on an ongoing basis, find it a profitable activity?

Ms. SEGER. Well, again, viewing CRA as I do, as the broad-based provision of services to your whole community, then I think that's what banking is all about. Even if you didn't have a CRA act on the books, I think the good banks understand that the way to survive is by serving their community and keeping their customers happy. If they make too many unhappy, they're going to be gone.

So I think there's that angle. But there are special categories of loans and special categories of activities that certain banks, particularly in the big cities such as Detroit or St. Louis, have supported that are higher risk—let's say redeveloping some portion of a downtown area—but they have been willing to go in and take that risk and they have assumed that if they underwrite these loans properly that they can still do a good job and come out whole.

Now there are some of these loans that don't pan out and there are others that work very well. In fact, it was said in the law that passed in 1977 that these loans still have to meet the standards of safety and soundness. In other words, we cannot turn these institutions into branches of the Salvation Army.

Senator BOND. You're not making this a charitable contribution.

Ms. SEGER. No.

Senator BOND. There's no reason why the CRA required community involvement ought to be at a loss or anything other than a reasonable profit. So this is a profit-making venture which can be pursued under the CRA?

Ms. SEGER. You hope so. As I said, sometimes after the fact——

Senator BOND. Sometimes you do it well and sometimes you do it poorly, but you're not looking at it and it's not your view that in administering this act that banks would be required to take on unprofitable business but just make the effort to gain profitable business by extending credit in these areas in their own community.

Ms. SEGER. Exactly.

Senator BOND. What do you think of the suggestions that some witnesses have made and some people I've heard discuss it say that the scope of the CRA ought to be broadened to include other financial entities such as mutual funds, insurance companies, mortgage brokers?

Ms. SEGER. Well, I believe in equitable treatment between and among financial institutions that have to compete with each other. So looking at it in that way, depository institutions such as banks and savings and loans do have a disadvantage here because they are hit with these specific requirements and all the costs that go with them, while the folks who compete with them in many of these lending activities play by a different set of rules. And that is not fair.

Now whether or not I feel that just taking the existing CRA and extending it to sales finance companies and American Express and folks like that, who are interested in having the banks do all this good work, I don't know if that would do it.

Senator DIXON. Jurisdictionally, how would we do that? It's an interesting concept.

Ms. SEGER. You mean in legislative terms or in regulatory terms?

Senator BOND. We could probably do anything we could get away with.

Senator DIXON. Well, I guess we can do anything we can get away with, but the Senator's question intrigues me, but you don't have any jurisdiction over those folks.

Ms. **Seger**. No. We don't regulate the money market mutual funds. That's the job of the SEC. And I believe that the sales finance companies are floating around out there without any babysitter at the moment.

Senator **Bond**. The savings and loan has a CRA requirement.

Ms. **Seger**. Oh, yes. Savings and loans are included right now. The Federal Home Loan Bank Board signed off on our new policy statement. But it's mainly nondepositories such as sales finance companies, pension funds, life insurance companies who are not covered, even though—all those folks make loans.

Senator **Bond**. Mr. Chairman, no further questions.

Senator **Dixon**. I thank my distinguished friend from Missouri. Governor, you have been very, very helpful and if you would accommodate this committee by sending to us, again I say, just a very brief position on each of the points you made and why, and particularly I'd like you to stress that numerical business, why you think that's a bad idea, because there'll be some issue in that I'm sure here.

You've been very helpful. We thank you, Governor.

Ms. **Seger**. Thank you. We would love to help in any way we can.

Senator **Dixon**. Thank you. I'm sure we will consult with you as we get to the conclusion of this.

Ms. **Seger**. OK.

[Response to Senator Dixon request of specific comments on the provisions in S. 909 follows:]

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MARTHA R. SEGER
MEMBER OF THE BOARD

July 21, 1989

The Honorable Alan Dixon
Chairman
Subcommittee on Consumer and
Regulatory Affairs
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

During the June 7 hearing on the Community Reinvestment Act (CRA), before your Subcommittee on Consumer and Regulatory Affairs, you requested the Federal Reserve's specific comments on the provisions in Senator Metzenbaum's bill, S. 909. I am pleased to provide the following response.

The Board supports the general concept of requiring regulatory agencies to prepare and publicly disclose written evaluations of institutions' CRA performance. We believe that this would be fully consistent with the thrust of the CRA policy statement issued in March by the four federal financial institution supervisory agencies, and would promote the early start of a constructive dialogue between an institution and members of its community about its CRA record.

However, the CRA evaluations that we support would summarize the examiner's findings and conclusions, and would provide supporting information related to the CRA assessment factors. They would not be the same as the examination reports themselves. Nor would they divulge material from the examination report which must be treated confidentially--such as information about the financial condition of the institution, and any sensitive information about its employees, customers, or members of the community.

Senator Metzenbaum's bill, however, can be read to require the agencies to make public the examination report itself--not a summary. Additionally, the bill sets out criteria for information that can be included in the confidential section of the report and further prohibits disclosure of this information to the depository institution or the public except in unusual circumstances. The Board opposes these provisions because we believe it is important to effective supervision and communication that examiners have a separate and confidential avenue for conveying the facts and conclusions of their reviews to the institutions.

The Board also opposes disclosure of institutions' numerical CRA ratings, as required in S. 909. At the very least, release of the numerical rating would divert attention from the more important and thorough information contained in a narrative summary of the examiner's findings. The rating systems for examinations were developed as a supervisory shorthand to enable us to know which banks need closer attention. The rating is not self-explanatory and, more importantly, we believe that there is also a potential for undermining public confidence in the safety of deposits in an institution if an adverse CRA rating were to be misunderstood as a reflection on that institution's financial soundness. In our view we can accomplish the purpose of this provision and avoid this risk by publishing a summary assessment of an institution's performance under the CRA.

Finally, the Board opposes the requirement in S. 909 that CRA evaluations be focused on three specific types of credit--loans for low and moderate income housing, small business, and small farms. Such a requirement is inconsistent with the Community Reinvestment Act, which does not require any specific type of lending. Since communities and banks differ, and because many other lending activities can contribute to community revitalization, we believe it would be unwise for the statute to place primary focus on a few enumerated types of lending.

I hope this information is helpful to your Subcommittee. Please let me know if I can be of further assistance.

Sincerely,

Martha R Seger

Senator DIXON. The first panel is, I am told, a panel on success stories. We'll see. Ted Wysocki, executive director, Chicago Association of Neighborhood Development Organizations, with Robin Foote, senior vice president of the First National Bank of Chicago; Charles Clement, senior vice president of Landmark Bank in St. Louis, with Mary Ann Cunningham, banking committee chair, Association of Community Organizations for Reform Now, ACORN, in St. Louis; and Charles Grice, Community Reinvestment Institute in San Francisco.

This is a panel obviously selected to satisfy the chair and the ranking member. Chicago and St. Louis. I don't know how San Francisco snuck in here. I'd like to yield for a moment to the ranking member from Missouri for his statement regarding this hearing.

OPENING REMARKS OF SENATOR BOND

Senator BOND. Thank you very much, Mr. Chairman.

I am delighted that you've invited witnesses from St. Louis as well as Chicago to discuss the Community Reinvestment Act. We'll have to check the staff to find out how other areas were represented as well, but we are today going to hear a discussion by representatives of Landmark Bank and ACORN. They formed a partnership that has resulted in increased flows of credit to low and moderate income neighborhoods in St. Louis.

I want to offer my special thanks to Charles Clement and Mary Ann Cunningham for coming to Washington to share experiences with us. I think that the stories that these witnesses from St. Louis and Chicago have to tell will be very instructive to all of us.

Most of the debate about CRA here in Washington consists of groups casting aspersions on each other's motives and refusing to listen. The fact is that banks do have a large stake in the economic well-being of their communities and community groups can benefit from the banks' financial expertise.

The success stories that we're going to hear about today in St. Louis and Chicago illustrate what can happen when people lower their voices, look at their common interests, and work together for the good of the community.

I look forward to the testimony of the witnesses and I thank the chair sincerely for your generous indulgence.

Senator DIXON. And I thank the distinguished Senator from Missouri.

Ladies and gentlemen, we follow a 7-minute rule on the testimony. Naturally, your entire testimony will be reproduced in the record in full. Would you kindly subscribe to the 7 minutes. There's a green light there and when you're running out it gets yellow and when it gets red all kinds of things begin to fall out of the ceiling and stuff like that.

Mr. Wysocki, we are delighted to have you here.

STATEMENT OF TED WYSOCKI, EXECUTIVE DIRECTOR, CHICAGO ASSOCIATION OF NEIGHBORHOOD DEVELOPMENT ORGANIZATIONS

Mr. Wysocki. Good morning, Senator Dixon and Senator Bond. I appreciate the opportunity to share with you a good news story from Chicago and my personal observations from almost 15 years of organizing for neighborhood development.

I must disclose that I spent 10 years working with the National Training Information Center and its executive director, Gale Cincotta.

Five years ago I accepted my current position as executive director of the Chicago Association of Neighborhood Development Organizations, CANDO, as we refer to it, after successfully completing negotiations with First Chicago, Harris Trust and Northern Trust, to establish their neighborhood lending programs. These agreements have become national models of how financial institutions and neighborhood organizations can be working partners in revitalizing their local communities.

First, let us be clear that the Community Reinvestment Act is the reason that these agreements were made.

Second, these agreements were reached because good faith negotiations occurred out of a mutual commitment to our fine city of Chicago. We approached the banks with the prospect of new business and we earned their respect for our neighborhood revitalization efforts.

The true test of our mutual success is measured by the fact that all three of these institutions have recently renewed their neighborhood programs for another 5 years with increased lending commitments. After lending over $125 million to Chicago neighborhoods, First Chicago, Harris and Northern are pledging to make another $225 million available. That's good business for those banks.

Let me describe to you the product that our partnership is delivering to Chicago's neighborhoods. Besides single family mortgages and home improvement loans, these programs have been essential in providing long-term mortgages for multifamily housing, for affordable housing in Chicago's neighborhoods.

The organization which I direct, CANDO, is a certified packager for the programs on the commercial side. We package loans for business expansion and retail development. Long-term real estate loans at preferable pricing has been instrumental to our industrial retention and our commercial attraction efforts in Chicago.

We also package loans for mixed-use properties which have both apartments and storefronts. Before these neighborhood lending programs, no one wanted to lend on these buildings. S&Ls didn't like them because of the storefronts and banks didn't like them because of the apartments. This is a whole new lending product that we're doing in Chicago.

To date, CANDO has packaged over 80 loans for $29 million. Half of these loans were for mixed-use real estate. Our members have helped broker over 300 loans for $40 million. With 70 community-based members and another 70 affiliate members, CANDO is the Nation's largest citywide coalition of neighborhood organizations. We are celebrating our tenth anniversary this year and would like to share our anniversary report with anyone who's interested.

Senator DIXON. I wonder if you would put that report in the record for us.

Mr. WYSOCKI. I'd be happy to. I just didn't know how well it would reproduce.

Senator DIXON. Thank you.

[Insert of CANDO anniversary report did not reproduce as expected.]

INVESTMENT IN NEIGHBORHOOD DEVELOPMENT

Mr. WYSOCKI. I think one of the things that we have shown is that investment in neighborhood development is money well spent. Every public dollar—and I wanted to stress this for the sake of this committee—every public dollar invested in a neighborhood development project yields $4 in additional project investment from private sources. Moreover, development initiated by our members often stimulate other private investment in the community increasing the total value to as much as $25 for every single public dollar. This development stimulates Chicago's economy as a whole, returning $28 in new tax revenues for each public dollar invested.

CANDO members currently have over 40 deals worth more than $200 million in the pipeline, awaiting resources to complete the job. More than 25,000 jobs could be affected if financing for business expansion continues.

This is the product that we are delivering in Chicago through these neighborhood lending programs and with Federal programs such as the Community Development Block Grant.

CRA has been a critical tool in this success, but let me differ from the previous witness that I think it's been despite the Federal regulators. On March 22 and 23, 1988, this Senate Banking Committee held hearings on CRA. Clear evidence was presented last year that the regulators had not been doing their job of enforcing this law and there were expectations for improvements. Yet when the regulators revised their CRA statement 1 year later, March 21, 1989, they continued to put the burden of CRA enforcement on the community. Only 3 percent—you mentioned these figures already this morning, Senator—of institutions fail compliance. Over 95 percent are awarded the top two CRA ratings.

This year, as you know, Senator, the Federal Reserve finally denied an application, Continental Illinois. They denied this despite the fact that Continental had a productive and a community-acceptable program that filled the particular lending need. I would like to suggest that since Continental was denied, that every institution in this country who has done less should fail their CRA exam. I think Continental's denial sets a new benchmark.

While CRA was written as a result of home mortgage redlining, I do believe it's time to reinforce that economic development is part of community reinvestment as well. Good jobs make housing more affordable. Business lending creates more jobs and shuttered factories are as serious for our neighborhoods as vacant homes.

I mention in my testimony two of our members down in southeast Chicago, South Chicago Savings Bank, whose chairman is Jim Fitch, who you know, Senator, and The Southeast Chicago Development Commission. They had a problem with the Federal Reserve over their CRA rating and while, sure, they are going to do more in terms of housing, this institution is an example for the country of a local institution that's been dedicated to improving the local economy of their community. They are currently working on a resource recovery industrial park which will be a $15 million investment and 1,100 jobs and none of this activity was considered by the Federal Reserve in their CRA review.

I believe CRA would work better if there were improvements at the examination stage. However, let me be clear that I do not believe that a renewed focus on CRA exams should deny a community group's right to challenge at the application stage. That right must persist. But if the exams were conducted with more competence and clarity of standards, institutions would be better able to respond and partnerships would be encouraged and communities would benefit and institutions would be able to undertake new ventures without fear of having their applications challenged.

SUGGESTIONS TO IMPROVE CRA EXAMS

The first improvement in exam procedures I would suggest is public notice of CRA exams. Community groups would then be able to file timely comments on the institution's performance. And I again will differ from the previous witness. I think the most significant improvement the Congress could make would be to pass legislation to require public notice of CRA ratings. If ratings were disclosed, it would reveal on a case-by-case basis the thoroughness of the regulator's exam. It would reveal the absurdity of a bank with no community programs receiving the same rating as my colleagues in First Chicago or Southshore Bank, to give another illustration in Chicago, that are national leaders in neighborhood lending.

A comment period could be provided for groups to challenge the proposed rating leading to fuller discussions between the regulators, institutions and the community.

Since I'm running out of time, let me just say, to respond to Governor Seger's response, I would think that not publicizing the CRA grade is like not sending the report card home. I think the difference between an A− and a B+, the difference between a 1 or a 2, is telling the institution you have to strive to do better. And I think it's an insult to the financial institutions in this country—two of them that are here today—who are doing meritous work not to be acknowledged to be on the dean's honor roll, to use the analogy there—or I guess in the case of the Federal Reserve, the governor's honor roll.

I have some other suggestions but let me stop there.

[The complete prepared statement of Mr. Wysocki follows:]

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Chicago Association of
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32

The Community Reinvestment Act & Economic Development in Chicago's Neighborhoods

Testimony before the
Subcommittee on Consumer & Regulatory Affairs
of the
United States Senate
Committee on Banking, Housing & Urban Affairs

by
Ted Wysocki
Executive Director
Chicago Association of Neighborhood Development Organizations

June 7, 1989

EXECUTIVE SUMMARY

Testimony before the U.S. Senate Banking Committee
by Ted Wysocki, CANDO on June 7, 1989

The Neighborhood Lending Programs that have been so successful, in Chicago are a direct result of the Community Reinvestment Act (CRA). CANDO's ten-year history of neighborhood economic development reflect the public/private partnerships that we have been able to forge by demonstrating that neighborhood development generates a guaranteed return.

However, in the ten-year history of CRA, regulators have not provided serious and competent enforcement of this federal law. The burden of enforcement has consistently been placed on community organizations.

CRA would work better if there were improvements at the examination stage:

1) There should be public notice of CRA exams.
2) There should be public disclosure of CRA ratings with an opportunity for groups to challenge the proposed rating.
3) There should be better established standards for CRA performance that distinguishes institutions with model programs from those doing far less.

However, a renewed emphasis on CRA exams should in no way deny a community group the opportunity to protest during the application process.

Community reinvestment should be acknowledged by regulators to include economic development activities. To this end, Congress should legislate public disclosure of commercial loan activity.

The Community Reinvestment Act is a federal law which demands the respect of the financial industry and consequently requires serious and competent enforcement.

As we enter another decade and the second ten years of CRA, we all -- Congress, the regulators, the lending industry and neighborhood organizations -- must commit ourselves to work together to do deals: Deals that revitalize our neighborhoods and this country's economy.

Good morning Senator Dixon and other distinguished members of this committee. I appreciate the opportunity to share with you a "good news" story from Chicago and my personal observations from over fifteen years of organizing for neighborhood development.

In 1974, as I was finishing graduate school, I found myself doing extensive title searches for selected Chicago communities. This research was used a year later in hearings by this committee which led to the passage of the Home Mortgage Disclosure Act (HMDA).

I went on to spend over ten years working with the National Training & Information Center and its Executive Director, Gale Cincotta. During that time, there were many stormy debates with the American Bankers Association over the Community Reinvestment Act (CRA). There were many meetings with various regulators on how this significant federal law should be best enforced.

Five years ago, I accepted my current position as Executive Director of the Chicago Association of Neighborhood Development Organizations (CANDO) after successfully completing negotiations with First Chicago, Harris Trust and The Northern Trust to establish their Neighborhood Lending Programs. These agreements have become national models of how financial institutions and neighborhood organizations can become working partners in revitalizing their local communities.

You will also hear directly from First Chicago on their extensive neighborhood portfolio. But since I was present at the initial meeting on December 14, 1983 with their chairman, Barry Sullivan, let me share some of my observations on how this story came to be.

First, let us all be clear that The Community Reinvestment Act was the reason the meeting even took place. Prior to its passage in 1978, it was extremely difficult to raise such issues. During the tenure of First Chicago's previous chairman, we had to do so from the floor of the annual shareholders meeting, when we had their first disclosure report.

Second, the meeting was productive because good faith negotiations incurred out of a mutual commitment to our fine City of Chicago. We approached the bank with the prospect of new business and we earned their respect for our neighborhood revitalization efforts.

This common self-interest has led to the on-going partnership that is reinforced at every quarterly review board meeting where loan progress is reviewed, problems are resolved, and future marketing efforts planned. The true test of our mutual success is measured by the fact that all three of these institutions have recently renewed their neighborhood programs for another five years with increased lending commitments. After lending over $125 million to Chicago's neighborhoods, First Chicago, Harris and Northern are pledging to make another $225 million available.

Let me next describe for you the product that our partnership is delivering for Chicago's neighborhoods. Besides single family mortgages and home improvement loans, these programs have been essential in providing long-term mortgages for multi-family housing. For example, the Guyon Hotel on Chicago's Westside was rehabilitated by Bethel New Life using bridge financing from First Chicago. These 114 units of affordable housing required over $3 million in public subsidies but they also required a long-term mortgage from Harris Trust.

The organization, which I direct [CANDO], is a certified packager for these programs on the commercial side. We package loans for business expansion and retail development. Long-term real estate loans at preferable pricing have been instrumental to our industrial retention and our commercial attraction efforts in Chicago.

We also package loans for mixed-use properties, which have both apartments and storefronts. For those of you not familiar with Chicago, every main street in every neighborhood is inundated with such properties. Before these neighborhood lending programs, no one wanted to lend on these buildings. S&Ls didn't like them because of the storefronts. Banks didn't like them because of the apartments.

However, these buildings are the backbone of our communities. As you drive Chicago's main streets, your perceptions of a neighborhood's vitality are formed on whether such buildings are deteriorated or are in good condition. Mixed-use properties are entrepreneurial opportunities for minorities and recent immigrants to own their place of business and living quarters.

To date, CANDO has packaged over 80 loans for $29 million. Half of these loans were for mixed-use real estate. CANDO members have helped broker over 300 loans for $40 million.

With 70 community-based members and another 70 affiliate members, CANDO is the nation's largest citywide coalition of neighborhood organizations. We are celebrating our tenth anniversary this year and would like to share our Anniversary Report with anyone interested.

Over the past ten years, CANDO members have had direct ownership roles in the development of more than $50 million in commercial and industrial real estate. Our support to businesses has created 5,000 jobs and retained another 75,000. CANDO's network has assisted in the start-up of 1,000 businesses, 50% being minority- or woman-owned.

From this ten year history, we have proven that investment in neighborhood development is money well spent. Every public dollar invested in a neighborhood development project yields $4 in additional project investment from private sources. Moreover, development initiated by CANDO members often stimulates other, unrelated private investment, increasing total value to as much as $25 for every single public dollar. This development stimulates Chicago's economy as a whole, returning $28 in new tax revenues for each public dollar invested.

CANDO members currently have over 40 deals worth more than $200 million in the pipeline awaiting resources to complete the job. More than 25,000 jobs could be affected if financing for business expansion continues. This is the product that we are delivering in Chicago through these Neighborhood Lending Programs and with federal programs such as the Community Development Block Grants.

The National Training & Information Center can point to over $2 billion in neighborhood lending commitments from 70 financial institutions in dozens of cities. The Community Reinvestment Act has been a critical tool in this success but its been despite the federal regulators. In the ten year history of this federal legislation, regulators have never taken this intent of Congress seriously. When Paul Volcker was the chairman of the Federal Reserve Board, he didn't even know what this federal law was that he was to enforce.

On March 22 and 23, 1988, the Senate Banking Committee held hearings on CRA. Clear evidence was presented that the regulators had not been doing their job of enforcing this law and there were expectations for improvements. Yet, when the regulators revised their CRA Information Statement one year later on March 21, 1989, they continued to put the burden of CRA enforcement on the community.

Only 3% of the financial institutions reviewed fail compliance and over 95% are awarded the top two CRA ratings. The Federal Reserve finally denied an application this year, while ignoring that Continental Illinois had a productive and a community acceptable program that filled a particular lending need. Since Continental was denied, then every financial institution in this country who has done less should fail their CRA exam.

While CRA was written as a result of the home mortgage redlining fight, it is time to reinforce that economic development is as critical to community reinvestment. Good jobs make housing more affordable. Business lending creates more jobs. Shuttered factories are as serious as vacant homes.

Since the regulators do not understand community reinvestment, they certainly do not appreciate the challenge of economic development. Two of CANDO's members, the Southeast Chicago Development Commission and the South Chicago Savings Bank, have spent the last ten years working to improve their local economy -- one of the hardest hit in the country over the last decade.

The Southeast Chicago Development Commission has packaged $13 million in small business financing. They are currently developing a Resource Recovery Industrial Park which will entail a $350 million investment and create 1100 jobs when fully completed. Jim Fitch, chairman of South Chicago Savings Bank, founded the Commission, served as its president, and has provided increasing financial support to the Commission's economic development activities.

There are few local financial institution in the country who can present such a decade of support for their community. Yet, the Federal Reserve examiners did not count this record worth anything when conducting their compliance exam. With 35% unemployment in the mid-80s, the demand for housing mortgages didn't lead to high mortgage lending. Could the bank do more housing loans? They are trying. Was the bank correct in prioritizing economic development? Certainly, but the Fed examiners never considered that question.

I believe that CRA could work better if there were improvements at the examination stage. However, I do not believe that a renewed focus on CRA exams should deny a community group's right to challenge at the application stage. That right must persist.

But if examinations were conducted with more competence and clarity of standards, institutions would be better able to respond; partnerships would be encouraged; communities would benefit; and institutions would be able to undertake new ventures without fear of challenges.

The first improvement of examination procedures would be for public notice of CRA exams. Community groups would then be able to file timely comments on the institution's CRA performance.

The most significant improvement that Congress could make would be to pass legislation to require public notice of CRA ratings. I know that the House Banking Committee narrowly rejected such an amendment proposed by Representatives Gonzalez and Kennedy. That vote was unfortunate and, perhaps, unappreciative of how such disclosure of CRA ratings could improve both the examination process as well as offer better encouragement to the private market.

If CRA ratings were disclosed, it would reveal on a case-by-case basis the thoroughness of the regulators' exams. It would reveal the absurdity of a bank with no community programs receiving the same rating as a First Chicago or a South Shore Bank who are national leaders in neighborhood lending. A comment period could be provided for groups to challenge the proposed rating, leading to fuller discussions between the regulator, the institution, and the community. Such discussions around the examination may lead to new partnerships and eliminate the necessity for concern around an application for new privileges.

Another improvement necessary is better established standards for CRA performance. With all of the community programs established over the last five years, the regulators should be able to set model programs for various sizes of institutions. Let the market dictate target goals. Whichever institution has the best program in their size range sets the expectations necessary for a top rating against which other institutions are judged.

The inability of the regulators to clarify performance expectations does not assist financial institutions in meeting their communities' credit needs. The inexperience of CRA examiners does not induce respect on the part of the industry nor achieve the objectives of Congressional intent. We have worked to professionalize the field of neighborhood development. The regulators can strive to do the same.

My final recommendation is to extend the Home Mortgage Disclosure Act to include commercial loans. This nation's economy runs on commercial loans. Community reinvestment must include analysis of how well business credit needs are being met.

This does not have to be a burdensome requirement. Call reports that financial institutions are already required to provide the regulators will suffice with minor changes. It would be helpful to have better definitions that distinguish between real estate loans for multi-family housing and real estate loans for a business facility. Data entry that distinguishes a 90-day working capital loan that is rolled over as not being a new loan would clarify the actual number of businesses being provided financing.

Call reports are commonly accepted by the industry as a price of doing business. Fines for failing to report underscore the seriousness in which they are regarded.

The business component of the Chicago program would not exist if we had not had commercial disclosure required of banks holding city deposits. That data showed us that in the three years from 1979 to 1981, First Chicago's commercial loans were so concentrated within the City of Chicago that 81% of the neighborhoods received only 7% of their commercial loans. Today, First Chicago proudly markets that their commercial loans are available in all 77 neighborhoods, proclaiming: "We put you first, Chicago!"

In closing let me stress the following:

- o The Community Reinvestment Act is a federal law which demands the respect of the industry and consequently requires serious and competent enforcement.
- o "Community Reinvestment" should be acknowledged by the regulators to include economic development activities.
- o Congress should legislate public disclosure of CRA ratings and commercial loan activity.

Our experience in Chicago demonstrates how neighborhood development is a guaranteed return and good business for financial institutions. Communities throughout this country need reinvestment, which requires the formation of partnerships with lending institutions to undertake neighborhood development.

As we enter another decade and the second ten years of CRA, we all -- Congress, the regulators, the lending industry and neighborhood organizations -- must commit ourselves to work together to do deals: Deals that revitalize our neighborhoods and this country's economy.

Thank you for the invitation to share my thoughts on these matters.

For the record, I have attached supplemental comments from Gale Cincotta which stress her support for commercial loan disclosure and her opposition to the Federal Reserve's new rules to prevent community groups from using the application process for CRA protests.

Chicago Sun-Times

CHICAGO SUN-TIMES
FRIDAY, MARCH 3, 1989

Resales/Rentals

PAGE 41

Banks re-enlist in neighborhood projects

By Thomas Kelly
Real Estate Editor

Renovation of this mixed-use building at Wrightwood and Cicero avenues was financed by the Northern Trust Co.'s Neighborhood Lending Program.

With a $90,000 loan from the Northern Trust Co.'s Neighborhood Lending Program, the Staff family renovated two apartments and three storefronts in a Northwest Side building.

Doing most of the work themselves, family members put up walls, made cabinets and rewired the electrical system in the building at Wrightwood and Cicero avenues.

The family, which emigrated from Romania five years ago, now lives in the two apartments and runs an auto body shop, an upholstery business and a fast-food restaurant from the three storefronts.

The 20-year loan, made in 1987, is from the $153 million committed by three major Chicago banks in 1984 for housing, commercial and industrial projects in low- and moderate-income Chicago neighborhoods.

In recent months, two of the lenders have increased their commitments, and the third, happy with the results, is evaluating the future.

"Reinvesting in these neighborhoods works," said Gale Cincotta, a community leader who has spearheaded the movement for reinvestment in Chicago and around the country. "We're looking forward to more success with this bigger, renewed commitment—and also to the continued growth and development of the neighborhoods."

Housing loans are made in targeted portions of the city, said Ted Wysocki, executive director of the Chicago Association of Neighborhood Development Organizations. Roughly 75 percent of the city would qualify, he said.

Businesses anywhere in the city are eligible.

"Any economic development is a benefit to the whole city," Wysocki said.

The latest commitment came last week when Northern Trust Co. pledged $25 million over the next five years. Nearly all of the $18 million Northern committed to its Neighborhood Lending Program in 1984 has been loaned out.

Also, Northern Trust has made a $500,000 grant commitment over the next five years to neighborhood revitalization programs, particularly those related to housing and economic development.

"We have funded more than 100 mortgages in this program with more than 900 housing units and a number of other mixed-use real estate projects," said David W. Fox, Northern Trust's president and chief operating officer.

Since 1984, the program has made $16.2 million in loans for housing, small businesses and mixed-use real estate projects in 3[illegible] Chicago communities including Uptown, Kenwood and South Lawndale.

In November, Harris Bank announced it was committing an additional $50 million over the next five years. Its initial commitment was $35 million.

Also, the Harris Bank Foundation will award $600,000 in grants.

"It's been a genuine partnership with the community groups identifying these loan opportunities to us," said B. Kenneth West, Harris chairman and chief executive officer.

The First National Bank of Chicago, the largest contributor in 1984 with $100 million, is evaluating its future course.

"First Chicago has been tremendously pleased with the continued progress and success of the Neighborhood Lending Program and with the relationship the bank has developed with the community and the community with the bank," said Laurie Glenn, bank spokeswoman.

Of the $153 million in initial commitments, more than $100 million was earmarked for housing, both single-family and multifamily, Wysocki said. The other funds are

Turn to Page 43

Proud CANDO eyes future

In the 10 years since its founding, CANDO has helped put together financing for 73 deals ranging from $3.6 million for the purchase of a portion of the Fulton Market to $90,000 for the renovation of a storefront-apartment project.

In the next 10 years, the Chicago Association of Neighborhood Development Organizations has even bigger plans.

"We've seen the growth in the number and capacity of all the neighborhood organizations," said Ted Wysocki, the group's executive director. "We're going to see an increased demand for financing."

As a result, the coalition of 70 neighborhood-based organizations is launching a "Neighborhood Investment Campaign"—a series of proposals to fund economic development in Chicago through the 1990s.

"The commitment of banks like Northern, Harris and First Chicago does raise the challenge of what the city is going to put in our neighborhoods," Wysocki said.

"If someone agrees to renovate a factory, there needs to be public money to fix the viaduct for the truck to get to the factory."

So, CANDO is proposing a $64 million Economic Development Financing Bond to assist in acquisition of property for industrial and retail projects.

It also is recommending that 10 percent of city-owned commercial and industrial properties be transferred to neighborhood projects in each of the next four years.

All together, the Neighborhood Investment Campaign proposals add up to $195 million in development funding to stimulate neighborhood economies and create new jobs.

"We have the human infrastructure, and we have the land, and we have the private money," Wysocki said. "We need the public dollars as well."

Banks are happy with community investment

Continued from Page 41

for small-business loans and mixed-use projects.

"The success of the lending program shows that lending in these neighborhoods is good for the neighborhoods and is good for business," said Cincotta, executive director of the National Training and Information Center in Chicago.

Owners can receive assistance in preparing applications, in lobbying with the lender and in dealing with state or city agencies from groups such as the Chicago Rehab Network, Chicago Association of Neighborhood Development Organizations and the Greater Southwest Development Corp.

For information about the neighborhood lending programs:

- For business and mixed-use loans, call the Chicago Association of Neighborhood Development Organizations at 845-9646.
- For multifamily housing loans, call the Rehab Network at 663-3936.
- For single-family housing, call the banks directly.

Chicago Sun-Times

CHICAGO SUN-TIMES, Saturday, March 11, 1989

Development group sure that it CANDO

Where your average Joe might see derelict buildings grounded in downhill neighborhoods, Ted Wysocki sees a rebirth of the Emerald City.

When others say cannot, neighborhood wizard Wysocki chants "CANDO."

And the bearded executive director of the Chicago Association of Neighborhood Development Organizations (CANDO) would like to take you down his yellow brick road to any one of Chicago's 100-plus neighborhoods.

"A Chicago neighborhood is a place not only to live," said Wysocki, a Logan Square resident, "but a place to shop and to work. We have gotten away from that and it has hurt. The city was built on mixed use."

Wysocki, 39, believes mixed residential and commercial use of buildings is needed to revitalize dying areas and support those already thriving.

"People need shoes, clothes, groceries—no matter where they live," he said. "Why buy them out in the suburbs?"

CANDO is the nation's largest coalition of neighborhood economic development organizations. From nine original groups, it has grown to 70 neighborhood-based and 70 citywide organizations.

"Neighborhood organizations have received a bad rap lately," said Wysocki. "Some say the groups are against development. What hasn't been told is how they are organizing for development."

The organizations' collective power is the hope and strength of the city.

"We have a legacy that if you wanted something, you had to organize to get the mayor's attention," said Wysocki. "The city has a history of strong neighborhood organizations. And the number is growing."

One collective idea from a 1984 CANDO brain-storming session was promoting neighborhood virtues to outside retailers and industry.

"We were having limited success in getting major commercial retailers and developers for neighborhood projects," said Wysocki. "So we made a homemade portfolio of 17 neighborhoods and went to where retailers were gathered."

By 1986, their inspiration became the annual Neighborhood Retail Fair.

CANDO will showcase 41 neighborhoods to the world on March 23 at the International Council of Shopping Centers at the downtown Fairmont Hotel.

"We have a product to sell—Chicago's neighborhoods," said Martin Berg, CANDO assistant director. "People are buying it. It is just a matter of introducing them to the idea that opportunities exist."

The city, Wysocki said, can be very competitive because retail industry has

NEIGHBORS

John Stebbins

SUN-TIMES/Tom Cruze

Ted Wysocki is executive director of the Chicago Association of Neighborhood Development Organizations.

But don't think CANDO wants to turn the city into one big shopping mall infested with gum-popping teenagers.

"The key is getting commercial strips revitalized through mixed use," said Wysocki. "Perceptions are based on what people see when they drive along these streets."

Three years ago, CANDO helped revitalize a large building in Chatham. Through mixed use, it now contains 60 apartments, 20 offices, 12 retail stores, a clinic and a bowling alley.

"It's a key neighborhood building," said Wysocki. "Such buildings offer opportunities to immigrants and a chance at the American Dream."

CANDO has tackled the thornier problem of a shrinking industrial base. Again, intelligent use of existing structures is the key.

"No company today wants an eight-story building," he said. "We split the building so eight companies can share it. It's cheaper and the building isn't abandoned. Industry is important to Chicago's future."

This month marks the 10th anniversary of CANDO. To celebrate, it has launched a neighborhood investment campaign to fund grass-roots economic development.

"The city is about a total life environment," said Wysocki. "It's great that downtown is being revitalized, but we are missing the point if we forget why Chicago was built the way it is.

"Chicago is the hub of the country. And the spokes of that hub are the neighbor-

Sunday
Chicago Sun-Times
APRIL 30, 1989

CANDO greens up city's grass roots

By M. W. Newman

Joel Bookman has a city planning degree but ran a pizza parlor and worked 16 hours a day for five years.

Dorris Pickens gave up schoolteaching for banking but got out of that, too.

James Capraro was a self-described "rabble rouser," a community organizer on the Southwest Side.

Now they are in the business of neighborhood economic growth. There probably isn't a more urgent business in Chicago. You don't make a lot of money in it, because the work is not-for-profit. The payoff comes in saving or helping to create jobs, business firms and housing and the lifeblood that goes with them.

Grass-roots economic coalitions have emerged as a Chicago specialty. The people who do the work are a civic "subculture," as Bookman puts it fervently—and he isn't kidding when he uses that word.

With dozens of other Chicagoans, he's an evangelist of the grass roots. The grass, against all the odds, appears to be getting greener as the coalitions come of age. No other city has as many.

Bookman directs the Lawrence Avenue Development Corp. in Albany Park. Pickens is with the Neighborhood Institute at 1550 E. 71st St., and Capraro guides the Greater Southwest Development Corp., 2358 W. 63rd St.

Their voices were among those heard last week at the 10th anniversary conference of the Chicago Association of Neighborhood Development Organizations (CANDO), a rising civic power. CANDO was founded 10 years ago by a few hardy souls in an Old Town pub. It has progressed so far that it is pressing for $195 million in city funding to carry on its work. The dollars would come from bond issues, federal grants and loans and the city's corporate fund.

SUN-TIMES/Al Podgorski

James Lemonides, who directs the Greater North Pulaski Development Corp., helped reopen the building that housed the Playskool plant at 4501 W. Augusta.

"We don't want a giveaway but an investment that will pay returns in tax revenues and jobs," said Ted Wysocki, CANDO's executive director.

The standing wisdom when CANDO started was that you couldn't bring back neighborhood stores or save manufacturing plants, but you could fight City Hall and you'd better fight investment "red-lining" of neighborhoods.

The infant CANDO mustered enough muscle to stave off a clout-heavy shopping mall that would have competed with 14 neighborhood shopping strips on the Northwest Side. But already that was the old CANDO, ready to take on the Establishment. The new one's 70 member groups are heavily involved in pushing neighborhood commercial growth—shopping and factories, along with housing.

About $50 million in projects have been realized and another $200 million worth are in the pipeline, said Wysocki. The banks have come around sufficiently to supply a $200 million investment pool. CANDO's affiliated members include such major Loop banks as First Chicago, Harris Trust and Savings Bank and Northern Trust.

"We have become developers," said Capraro. "I was a different person when I started."

There is still considerable doubt whether manufacturing can be saved in Chicago. The immense payrolls of old-line industry have vanished and the city continues to lose about 15,000 blue-collar jobs a year.

But CANDO teams have learned to marshal financing, marketing expertise, organizing skills, public and private linkage and the will to stay in the battle. By now there have been enough victories, even if most are fairly modest, to convince the groups they can make a difference despite massive shifts in the way the world makes a living. They have helped to launch about 1,000 business firms.

"Even if it's fingers-in-the-dike, and I don't believe it is," said Bookman, who is CANDO's president, "what would happen if we didn't do it?

"We're dealing with thousands of lives, homes, jobs. We know the global economy is changing, but there are more immediate concerns for people on Lawrence Avenue."

James Lemonides directs the Greater North Pulaski Development Corp., 4055 W. North. Industry is still lively in that part of town, and it was a tremendous jolt to the neighborhood when the Playskool plant on Augusta Boulevard shut down in 1984. About 700 jobs were lost.

Lemonides and his team sweated that one out for about four years. They came up with $550,000 as their portion of a successful $3.5 million deal to reopen the building as a home for half a dozen firms.

Some 450 jobs have been developed, according to Lemonides. Most of them average about $2 an hour less than the Playskool level of $6 to $6.50, he said. But that's better than a dead factory or another shopping mall, said Lemonides.

The CANDO strategy for the city's economy is to build on Chicago's strengths. As Wysocki defined it, that does not mean flashy new high-tech industries, as welcome as they might be.

Chicago's base, he said, includes "a diverse economy, a labor force, land, suppliers, transportation, location." CANDO wants a crack at the empty acres languishing on the city's tax rolls.

"The city has to be a key player," Wysocki said, with long-term funding of grass-roots growth.

"We know it has budget problems and that more federal dollars are not likely. We know we're pushing at the outer limits, but the city has to be creative and look ahead."

The CANDO program has been forwarded to Mayor Daley.

Senator DIXON. I assure you you will have plenty of time to expand on that, Mr. Wysocki, in the Q and A and your observations are very, very interesting. I guess, if the chair could be indulged in for a moment with respect to everything you've said, I think the way that this is supervised is key. We'll develop that in the Q and A in a minute. I don't know how much the grade means, but I would certainly say that it comes through very clear to this senator that those of you out there in the neighborhoods don't think that the evaluation process and the supervisory process is working very well right. I get that point.

Ms. FOOTE.

STATEMENT OF MARION R. FOOTE, SENIOR VICE PRESIDENT/DEPARTMENT HEAD, SPECIALIZED FINANCIAL SERVICES, FIRST CHICAGO CORP.

Ms. FOOTE. Mr. Chairman and members of the Subcommittee, thank you very much for the opportunity to speak today.

My name is Robin Foote and I'm a senior vice president of the First National Bank of Chicago. You have asked me to share with you how First Chicago, in conjunction with our community partners, has made CRA work well. We appreciate the opportunity to discuss the success of this program with you and are honored that you should invite us to do so.

Let me start with a bit of perspective. In the last year, First Chicago has greatly increased its commitment to its neighborhood lending program. Specifically, we have extended to 10 years and increased to $225 million our original 5-year $100 million program to fund loans to increase the quality and quantity of affordable housing and to revitalize small businesses in the Chicago area.

We have doubled our actual loan commitments, increasing them from $36 million to more than $75 million. Once fully funded, these loan commitments will finance more than 2,300 dwelling units and 100 commercial properties in Chicago's low and moderate income neighborhoods.

We have increased by $9.5 million our total commitments to fund loans to the Community Investment Corp., a consortium of 30-plus banks and savings and loans in the Chicago area making loans on a participative basis, and we have increased our share of that organization's line of credit which we manage by $2.5 million.

Finally, we have increased our contributions to community-based, not-for-profit development organizations and neighborhood advocacy groups by 25 percent, to at least $500,000 annually for the next 5 years.

None of these commitments would have been made if First Chicago were dissatisfied with the performance of the programs it has undertaken to meet the requirements of the Community Reinvestment Act. We attribute our success to five factors.

First, responsible leadership. Members from both First Chicago and community groups approached the task of creating this lending organization in the spirit of developing actionable constructive solutions to real problems of mutual concern. As a result, we established a true working partnership and have created a feeling of mutual trust and respect that did not exist 5 years ago.

Second, we approached the program with sound business principles. The program is designed to make a profit, albeit a modest one, and our community partners understand that this is essential if we are to stay in this business long term. Although we accept nontraditional forms of equity, we finance only up to the lesser of 80 percent of market or 90 percent of costs. Projects are evaluated by a small but extremely able team of professionals, using sound underwriting and credit criteria.

As a result, the business performs well. It has received continued resource commitment from First Chicago, and our staff are recognized leaders in CRA both in Chicago and nationally.

The third critical factor has been the availability of Federal resources. Many projects require funds in excess of that which a bank can prudently provide, given the project's anticipated cash flow. In such cases, it has been essential to have financing such as the low-cost community loans available under the Community Development Block Grant program to close the funding gap and ensure that rents remain affordable.

As you know, these funds have diminished greatly in recent years. As a result, fewer and fewer projects can be financed in spite of the substantial increase in private sector funding available for such projects.

The fourth factor has been that we adopted a multifaceted approach. Our program includes not only direct loans, but also investments through the Chicago Equity Fund, participation in and support of the Community Investment Corp., contributions to a wide variety of neighborhood organizations, and leadership in forums such as the Chicago Housing Partnership.

As a result, we are deeply familiar with housing issues from a wide variety of perspectives. As well, much needed agencies and institutions have sufficient resources to carry out their essential roles.

The final very critical factor has been the availability of skilled entrepreneurs. Chicago is blessed by a core group of developers who have chosen to dedicate some or all of their efforts to low and moderate income housing. At this point many are stretched thin. As a result, one of our most serious challenges is to continue to expand the supply of entrepreneurs in this field.

Mr. Chairman, I think that you can see from the above that our Community Reinvestment Act law is effective as written. In our opinion, however, it needs to be extended to other participants in the financial services arena, with particular attention to those who take deposits.

In addition, however, lenders should be required to serve all members of their communities. Thus, we believe CRA should encompass institutions such as mutual funds, insurance companies, mortgage brokers, investors and lenders, independent and captive finance companies, brokerage houses, and so forth.

Increasingly, these financial services providers look like banks. In many areas they compete directly with us. Yet, Mr. Chairman, they are not subject to CRA and do not acknowledge any responsibility to serve the relatively less-profitable credit and deposit needs of low and moderate income people and communities.

In view of the magnitude of the challenge facing all of us in ensuring decent and affordable housing for all Americans, we cannot afford to let these participants with their deep pockets and resources to take funds from our communities without commensurate reinvestment. Doing so only hampers the banking industry, making it a higher cost producer, less and less able to compete effectively with these other financial services players. Mr. Chairman, I urge you and your colleagues to consider embracing the notion that the cost of serving the credit and deposit needs of the public is compliance with CRA for all providers, including but not limited to banks. We believe that the focus of increased CRA compliance should be on those banks and others who have done the least to date. If everyone reaches the level of the leaders, then we can productively talk about raising the standard for all.

That concludes my oral testimony. Thank you for your attention. Now I would be glad to answer any questions you or your colleagues may have.

[The complete prepared statement of Marion R. Foote follows:]

TESTIMONY OF

MARION R. FOOTE

SENIOR VICE PRESIDENT/DEPARTMENT HEAD, SPECIALIZED FINANCIAL SERVICES

FIRST CHICAGO CORPORATION

BEFORE THE

U.S. SENATE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

OF THE

U.S. SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, D.C.

JUNE 7, 1989

TESTIMONY

Mr. Chairman and members of the Subcommittee, my name is Marion R. Foote. I am a senior vice president and head of the Specialized Financial Services Department in the Personal Banking Group of First Chicago Corporation, a bank holding company whose subsidiaries include The First National Bank of Chicago, American National Corporation, First United Financial Services, and the Gary-Wheaton Corporation, and Midwest Mortgage Services, Inc., all in the city of Chicago and its northern and western suburbs.

We are honored by this opportunity to appear before you to discuss First Chicago's Community Reinvestment Act experience, and what has led to our success.

By way of background, five years ago First Chicago started the Neighborhood Lending Program with an initial commitment of $100 million. To date, over $75 million has been utilized for the purchase and rehabilitation of more than 2300 residential and 100 commercial properties in low- and moderate-income neighborhoods in the Chicago area. On April 24, 1989, First Chicago announced that, between now and 1994, it will make available to lend at least $150 million for projects that increase the quality and quantity of affordable housing in the City's low- and moderate-income neighborhoods, or that help to revitalize small businesses located within the city. $25 million of this commitment will be carried over from the initial program, resulting in $225 million in funding over the 10 years from 1984 to 1994. We also announced that contributions to community groups for neighborhood development would be increased by 25% to at least $500,000 annually from 1989 through 1994.

When we created our neighborhood revitalization program, we sought to carve out for ourselves a leadership role in the community. We accepted the challenge of becoming a role model for the banking industry. As we look back over our experience, we have identified five factors that have enabled us to achieve this stature:

1. Responsible leadership: Both First Chicago and our community partners came together with a commitment to work together to find creative ways to help meet the need for affordable housing.

2. Sound business principles: It was agreed at the outset that the program would meet "safety and soundness" standards and contribute positively to the Corporation's earnings.

3. Availability of federal resources: Such resources have helped to close the funding gap on numerous projects, thereby leveraging private sector resources across a broader spectrum of deals and helping to keep rents affordable.

4. Multi-facted approach: We not only made direct loans, but also investment in and contributions to a wide variety of housing-related private sector programs, organizations, and agencies.

5. Availability of skilled entrepreneurs: The program could not operate without these individuals.

The following sections address each of these critical factors in greater depth. A final section outlines directions First Chicago urges you, Mr. Chairman, your colleagues on this Committee, and others on the Hill to consider to ensure that CRA achieves maximum possible benefits for the low- and moderate-income constituents whom it was designed to assist.

Key Factor #1: Responsible Leadership

In 1984, when the Neighborhood Lending Program was first developed, our goal was to establish with representatives from appropriate community groups, a true partnership that would work together to develop actionable and constructive solutions to real problems of mutual concern. The key here is that we focused on finding areas of common interest, as opposed to concentrating on issues which would pull us apart. Three factors motivated our interest in taking a leadership role in CRA:

- CRA is the Law: However, while this certainly played an instrumental role in our initial involvement, it has had little to do with our ongoing commitments since then.

- The needs are real: We recognized that our local communities were, in fact, starved for loan funds, and that, without these funds, troubled neighborhoods could not improve and good neighborhoods could decline.

- Effectively meeting the needs would be good for business: We understood that the program would enhance the economic health of our marketplace and that it could generate profitable business.

From their perspective, our community partners understood the power CRA vested in them as well as the need to find approaches that addressed their agendas in ways that were consistent with the Bank's goals. Further, they understood that the program needed to operate as a business, and that it should be profitable.

Working together with vision, courage, creativity, and patience, we designed a program that would benefit the less-advantaged citizens of Chicago, and we institutionalized it through two entities: (1) the Neighborhood Lending Division, which has a full-time staff of 7 and is responsible for the day-to-day review, evaluation, and approval/denial of loan applications; and (2) the Neighborhood Lending Review Board, which consists of a balanced mix of First Chicago personnel and community representatives. The Review Board meets quarterly and has ultimate approval authority for all projects that are counted toward meeting our $225 million loan commitment. As well, the Review Board provides advice and counsel on pricing, underwriting practices, program modifications, and certification of community organizations that wish to work with developers to prepare loan applications for consideration under the program. (We call such agencies "certified packagers.")

The Review Board provides an effective forum for an ongoing dialogue about the program and for discussing changes that are inevitably needed to keep up with evolving requirements. Board members are selected based on their demonstrated commitment to affordable housing and commercial development in Chicago's neighborhoods, their knowledge of the needs, their personal effectiveness as leaders in their respective areas, and their genuine interest in and willingness to work in a partnership mode to make the First Chicago Neighborhood Lending Program a role model for such programs in Chicago and nationwide. Community leaders currently serving on the Board include:

Gale Cincotta
Executive Director
National Training and Information Center

Elzie Higginbottom
President
East Lake Management, Inc.

Nina Klarich
President and Chief Executive Officer
Chicago Technology Park

Robert Lucas
Executive Director
Kenwood Oakland Community Organization

Uthman Muhammad
Executive Director
South Austin Madison Corporation

Mary Nelson
Executive Director
Bethel New Life, Inc.

Juan Rivera
Executive Director
Latin United Community Housing Association

Richard Turner
Senior Vice President
South Shore Bank of Chicago

Gerald Prestwood
Executive Director
Chicago Rehab Network

Ted Wysocki
Executive Director
Chicago Association of Neighborhood
Development Organizations

It would be misleading to suggest that First Chicago management and community leaders forged a smooth working relationship from the outset. Rather, we needed to learn to work together and to speak the same language. Early Review Board sessions were often acrimonious, but we learned to overcome our differences, as evidenced by the quotations below which were released in conjunction with the announcement of our Fifth Anniversary celebration and the expansion of our Neighborhood Lending Program:

> "First Chicago is a recognized leader in the area of community reinvestment, and I am delighted by the amount of funding the Bank is making available, particularly the increase in grants to community organizations. Chicago deserves national recognition for the success of the public/private partnerships that have been created in the last five years to address housing issues. These programs have benefited the city, its residents, and those participating in them."
>
> --Gale Cincotta, Executive Director
> National Training and Information
> Center

"We've borrowed money from First Chicago and intend to borrow more. We've forged a real working partnership between the public and private sectors on housing issues. More important, there is a feeling of mutual trust and respect which didn't exist five years ago. That's exciting."

--Mary Nelson, President
Bethel New Life, Inc.

"This shows how a bank can have an active commitment to the Community Reinvestment Act. The program is well balanced, with 30% of the loans made so far going to commercial and mixed use development."

--Ted Wysocki, Executive Director
Chicago Association of Neighborhood
Development Organizations

This evolution came about through a willingness to listen to each other's points of view and to allow the program to take shape over time. Loan growth has been exponential since the early years, principally because such volume has been facilitated through the effective dialogue that has been established between the parties:

$ Millions

	Number of Projects	Annual Commitment	Cumulative Commitment
1984	11	$ 1.4	$ 1.4
1985	29	6.7	8.2
1986	32	8.1	16.3
1987	74	16.9	33.2
1988	85	33.9	67.1
1989-March	23	9.0	76.1

Key Factor #2: Sound Business Principles

From the outset, both First Chicago and our community partners recognized the need to agree on the boundaries of what First Chicago--or any bank--could and, equally important, could not do in community lending:

- As financial intermediaries, banks can take deposits and make loans. Since they lend their depositors' funds (and these, in turn, are insured up to $100,000), they must have some arrangements for getting the money back with a high degree of certainty.

- In their fiduciary role, banks cannot:

  - Save a community with grants or gifts or below-market money
  - Make unsound loans
  - Make mismatched loans
  - Invest equity in projects.

Within these overall constraints, we have tried to approach community lending like any other business proposition. Specifically, we have sought to:

- Understand the unique financing requirements of Chicago's low- and moderate-income communities, particularly as they relates to community development needs.

- Develop loan products to meet those needs.

- Market these loan products effectively, without regard to any factor other than the ability to repay based on reasonable credit standards and realistic cash flow projections.

- Staff the Neighborhood Lending Division with knowledegable professionals who can deliver these products effectively.

Key elements of our Neighborhood Lending Program include the following:

- Qualifying neighborhoods: For housing, we target areas with average household income of 80% or less than the Chicago SMSA median. Small business loans may be made citywide.

- Project criteria: All projects require community endorsement. Housing projects also require a high standard of rehabilitation and affordable rents for residents of the neighborhood. Commercial projects are expected to create or save jobs.

- Underwriting criteria: Loan amounts cannot exceed the lesser of 80% of fair market value or 90% of cost. The balance must be made up in cash or an approved substitute--e.g., we may allow a developer to contribute his development fee. Or, the borrower may obtain equity from a source like the Chicago Equity Fund. All loans are made with recourse to the borrower's personal assets, except in the case of not-for-profit developers.

  Subject to these overall guidelines, we are as flexible as possible within the bounds of prudent banking practice, and we generally try to qualify each deal presented. (Since inception, we have approved roughly two-thirds of the deals that have been proposed.)

- Loan terms: Up to 30 years, but not longer than the useful economic life of the asset financed.

- Pricing: Loan pricing is, by its very nature, a creative aspect of the lending business. We have made available very favorable prices on loans for this program. For example, the Bank charges no points for loans that are brought to us by certified packagers. Rather, the packager charges and retains the points to defray its expenses. For other loans, points are charged at below-market rates. Most loan rates are variable, however, movement is limited by tight periodic and lifetime caps.

Of the more than 250 projects financed since inception, only one is seriously delinquent. An additional 2 loans are 90 days or more past due at this time. Together, these loans have aggregate balances of $680,000, or less than 1% of the face amount of deals approved to date under the program.

Since 1987, the Neighborhood Lending Division has made a positive contribution annually, although the amount is projected to diminish substantially in 1989 due to the impact of rising funding costs on spread income (the difference between interest income and interest expense), plus the impact of adherence to FASB 91 accounting standards. We are optimistic that, given the variable nature of the majority of our loans, this situation will be rectified as the loan rates adjust upward with time.

Key Factor #3: Availability of Federal Resources

Whenever a project's costs exceed estimated post-completion fair market value, there is a gap between how much financing the bank can provide and total project cost. If the gap is small and/or the borrower has substantial resources, this gap can be closed fairly easily. If not, additional funds are needed.

This is where federal funding becomes essential. The financing cannot be provided (as a loan) from the private sector because the lender would be in a subordinated position without sufficient cash flow to amortize his loan. Moreover, if conventional rates were charged for the whole project, rent levels easily could be driven beyond affordable levels.

Let me illustrate these points with an example:

- Project cost: $327,000
- Estimated Fair Market Value Upon Completion: $198,000
- FNBC Loan: $117,000 (60% of FMV)
- Owner's Equity: $35,000
- Financing Gap: $175,000

In this case, the borrower was able to obtain a low-interest (3%) second mortgage in the amount needed from the Chicago Department of Housing. As seen below, this financing not only closed the gap, it brought rent levels down to an affordable level:

Apartment Size	Rent Levels With $175K DCH Low-Interest Loan	Rent Levels With 100% Bank Financing
2 Bedrooms	$450/mo	$739/mo
3 Bedrooms	$550/mo	$839/mo

The affordability factor is the reason First Chicago's loan was only 60% of projected post-rehabilitation value. Any more conventional financing would have placed rent levels beyond the reach of area residents, thus necessitating that tenants obtain Section 8 certificates, for which there is an extremely long waiting list.

Why, you might ask, should this project be done at all? Shouldn't the post-rehabilitation market value exceed the rehabilitation cost? The answer is it often will not, because appraised value reflects the condition of the neighborhood and rental levels in the area. However, the cost of construction, labor, plumbing, electrical supplies, etc., is the same whether you are renovating an apartment building in an affluent market or a high-rise in a low-income neighborhood. Both the amount the developer can borrow based on his appraised value, and the rents he can charge, are constrained by the realities of the marketplace, whereas his costs are dictated by other factors. It is this financing gap which generates the need for subsidized financing.

Since 1977, the HUD budget has decreased dramatically in both absolute dollars and as a percentage of total Federal outlays:

	HUD Budget	
	$ Billions	% of Total Federal Budget
1977	$33.8	7.2%
1978	38.0	7.4
1979	31.1	5.5
1980	35.9	5.3
1981	34.2	4.6
1982	20.9	2.6
1983	16.6	1.9
1984	18.1	1.9
1985	31.4	2.9
1986	15.9	1.5
1987	14.7	1.3
1988	15.4	1.3

The results of this reduction are well known:

- Since 1981, the proportion of Americans who own their own homes has been decreasing, after increasing for 35 years in a row.

- The average 30-year old spends 44% of his or her paycheck on housing, versus 14% in 1949.

- One-fourth of the nation's poor spend more than 75% of their cash income for rent; 60% of the poor live in substandard housing.

- By the year 2000, we could lose most of the existing 1.9 million privately owned subsidized housing units.

For CRA to work, adequate funding must be available to leverage private sector resources to ensure that projects such as the one described above can be completed. Otherwise, we will fail to deal with the most severely disadvantaged Americans who are most in need of the benefits CRA can provide. Simply stated, housing must be afforded higher funding priority at the national level.

Key Factor #4: Multi-Faceted Approach

We supplement our direct loan program with a number of activities aimed at housing and community-based economic development. Principal among these are the following:

- Community Investment Corporation: First Chicago remains a leading participant in the Community Investment Corporation (CIC), a consortium of 30+ financial institutions cooperatively lending in Chicago through a non-profit mortgage banking firm. First Chicago works with CIC in three ways:

  - First, we have a $20 million commitment for the purchase of CIC participation notes used to fund mortgages, with a commitment to recycle that money as loans are paid back. This represents a $4.5 million increase in our commitment in the past year, and we account for 18.2% of the total pool (the largest share of any local institution).

- Second, we manage for CIC a $17.5 million participative line of credit, of which we provide $7.5 million on a "first in, last out" basis. This represents a $2.5 million increase since last year.
- Finally, to give CIC liquidity and to make further mortgage loans, First Chicago has purchased $9.7 million out of CIC's portfolio of seasoned loans. This represents an increase of $5 million versus last year.

Thus, taken together, our commitments to the Community Investment Corporation have increased $12 million in the last year.

- Chicago Equity Fund: First Chicago invests in the Chicago Equity Fund through its development subsidiary, the First Chicago Neighborhood Development Corporation. First Chicago has contributed $250,000 annually to the CEF since its inception in 1985.

  The Equity Fund supplies capital to not-for-profit housing developers focusing on low- and moderate-income development. The Equity Fund manages a pool of investment capital of approximately $25 million contributed by more than two dozen major Chicago-area corporations as investment partners. Returns to investors in all Equity Fund partnerships consist solely of tax benefits, the most recent of which have been made possible by the tax credit for low- and moderate-income housing development (LIHC) created by the Tax Reform Act of 1986.

  To date, the various CEF partnerships have invested a total of $21 million in neighborhood-sponsored low- and moderate-income housing. These developments represent a total of roughly 1,800 housing units throughout Chicago. Typically, CEF financing covers 20% of a project's total development cost, with a mix of conventional and subsidized funding covering the remaining project costs.

- Contributions to Community Organizations: Beginning in 1984, we shifted the focus of our foundation to make available more grants to community-oriented and neighborhood-based organizations, not-for-profit developers, and technical assistance groups such as the National Training and Information Center (NTIC) and the Chicago Association of Neighborhood Development Organizations (CANDO). Since that time, we have increased our grants to such organizations to a level of $440,000 in 1988, or $40,000 more than our stated goal of $400,000. In 1989, we will spend considerably more than $500,000, which level we have committed to sustain at least through 1994.

- Venture Capital Grants: Since 1985, we have provided more than $350,000 in restricted grants to non-profit organizations to provide equity for for-profit, wholly owned taxpaying corporate subsidiaries. While the results of this innovative program have not been all we had hoped, it has provided valuable lessons for future similar pursuits.

- Campaign for Responsible Ownership: Starting in 1984, First Chicago provided the first corporate support for the non-profit organizations who sought to revise the scavenger sale procedures for Cook County's tax delinquent properties. Since then, legislation has been passed that has helped to improve property tax collections and accelerate the transfer of tax-delinquent properties to low-income housing developers at little or no cost.

In addition to these activities, First Chicago is an active member of the Chicago Housing Partnership, which brings together public and private sector participants on a regular basis to discuss housing issues of mutual concern. Finally, our staff speaks frequently on CRA-related matters to other banks, community groups, municipalities, legislators, and anyone else with a legitimate interest.

Key Factor #5: Availability of Entrepreneurs

The availability of skilled entrepreneurs is the final critical factor which has enabled us to succeed in this program in Chicago. Our largest single borrower has done five projects with us and has total loans in the amount of $5.4 million. Five other borrowers individually have total loans in excess of $2 million with us. An additional 9 borrowers have loans in excess of $1 million. Ten of these 15 borrowers who constitute our largest customers, have multiple loans with us. This is both an advantage and a disadvantage. These individuals have strong track records and excellent reputations and we are confident of their ability to complete their projects on time and in budget. At the same time, however, more projects could be done if more entrepreneurs were available.

Opportunities to Enhance CRA Effectiveness

Mr. Chairman, members of the Subcommittee, First Chicago has accomplished its results under existing CRA legislation and with existing enforcement procedures. We view the clarification provided in the Joint Statement on the Community Reinvestment Act as a step forward, however, we do not believe additional legislation regarding banks' participation is what is called for at this time.

Rather, we think the most critical step to increase the effectiveness of CRA legislation is its extension to embrace all financial institutions who take consumer deposits and have (or should have) a responsibility for making credit available in their communities. Specifically, CRA should be extended to other participants in the financial services arena, with particular attention to those who take deposits. In addition, however, lenders should be required to serve all members of their communities. Thus, we believe CRA should encompass institutions such as mutual fund companies; insurance companies; mortgage brokers, investors, and lenders; independent and captive finance companies; brokerage houses; and so forth.

Increasingly, these financial services providers look like banks. In many areas, they compete directly with us. Yet, Mr. Chairman, they are not subject to CRA and do not acknowledge any responsibility to serve the relatively less-profitable credit and deposit needs of low- and moderate-income people and communities.

In view of the magnitude of the challenge facing all of us in ensuring decent and affordable housing for all Americans, we cannot allow these participants with their deep pockets and resources to take funds from our communities without commensurate reinvestment. Doing so, only hampers the banking industry, making it a higher cost producer, less and less able to compete effectively with these other financial services players. Mr. Chairman, I urge you and your colleagues to consider embracing the notion that the cost of serving the credit and deposit needs of the public is compliance with CRA for all providers, including, but not limited to, banks. We believe that the focus of increased CRA compliance should be on those banks and others who have done the least to date. If everyone reaches the level of the leaders, then we can productively talk about raising the standard for all.

Unless and until CRA is extended to these other financial institutions, which include among them giant corporations such as Ford, General Motors, Prudential-Bache, Sears, and American Express, they will remain at a competitive advantage relative to banks and savings and loans, who today must singularly shoulder the burden of these community responsibilities.

If some or all of these corporations prefer not to evidence their CRA involvement through lending commitments, these companies could:

- Agree to invest in loans produced by active CRA participants such as First Chicago or non-profit lenders like the Community Investment Corporation.
- Form an equity fund to provide development capital such as the Chicago Equity Fund.
- Make direct grants to community-based organizations.
- Arrange with banks to subsidize interest rates on certain types of loans.
- Develop delivery mechanisms that allow for products to be tailored to the specialized needs in areas where standard products are not appropriate.
- Accept lower margins on goods and services provided to low- and moderate-income people, just as the banks and S&Ls who are subject to CRA do on these commitments.

We believe expansion of CRA to all financial services participants is both necessary and appropriate. We urge you and your Subcommittee to consider legislation to this effect affirmatively.

In addition, while it is not directly under your jurisdiction, our efforts in community reinvestment would be greatly facilitated if your appropriate colleagues took action which:

- Reversed the long-term decrease in federal funding for low-interest loans and Section 8 rental subsidies.
- Ensured that the low-income housing credits, which make possible programs like the Chicago Equity Fund, are continued beyond 1989.
- Reexamined the Davis-Bacon Act for applicability to low- and moderate-income housing. Labor is a far more significant component of total cost than financing in determining the ultimate rent levels and, thus, affordability of housing. Union labor costs up to 30% more than non-union labor in most cities. This can make a real difference between housing that is affordable and that which is beyond the reach of many Americans.

Mr. Chairman, members of the Subcommittee, our community partners and we would be deeply grateful for any assistance you can provide in ensuring that your colleagues' legislative agendas include affirmative action on these issues.

State and local governments should also take steps to update their building codes, accelerate the restoration of property to the tax rolls, etc. Specifics need to be developed at the local level. However, leadership at the Federal level on the initiatives outlined above would go a long way toward encouraging all participants to combine in a spirit of cooperative problem solving around the issues of affordable housing in America.

ADDENDUM TO TESTIMONY OF MARION R. FOOTE

BASIC BANKING

Mr. Chairman and members of the Subcommittee, I would like to take a moment of your time to describe The First National Bank of Chicago's experience with basic banking products by briefly explaining Illinois' basic banking law and the banking products that First Chicago has developed.

As of July 1, 1986, Illinois banking laws have required financial institutions to offer basic banking transaction accounts to persons age 65 and over. The law states that the account must allow ten free checks a month and must not require a minimum balance. In addition, the opening deposit requirement cannot exceed $100.

In response to this law, First Chicago created the First Advantage Checking Account. This account meets the legal requirements and is available to all persons, regardless of age.

Consumers have been very responsive to the First Advantage Checking Account. First Chicago holds 25,400 accounts with an average balance of $600.

First Chicago has also developed a second basic banking product, called the Renaissance Checking Account which was introduced in April 1989. The Renaissance Checking Account is an expanded version of the First Advantage Checking Account and was designed for the checking needs of persons age 55 and over. This interest bearing account pays 5.25%, can be opened with an initial deposit of $100 or more, and does not have a minimum balance requirement. The account also features free unlimited check writing privileges and a free safe deposit box for one year. In addition, the First Chicago Visa and Mastercard annual $20 fee is waived. The Renaissance Account has not yet been actively marketed, but initial customers total 93 and maintain balances that average $4,400.

Senator DIXON. Ms. Foote, I find your testimony very valuable and want to take this opportunity while my ranking member of the subcommittee is here and the distinguished chairman of the whole committee is here to say, as a professional, one of the most enlightening experiences in my career has been to be at your institution when Gale Cincotta, representing the neighborhood groups, and the president of your bank and the chairman of your board and most of your executive officers all had this big party and celebrated the good work you're doing by putting hundreds of millions of dollars in the community and making them happy while you make a profit. That was one of my better days and I thank you for being here today.

I am delighted to recognize our distinguished chairman of the entire committee, who has honored us by coming to the subcommittee hearing.

OPENING STATEMENT OF CHAIRMAN RIEGLE

Senator RIEGLE. Thank you, Chairman Dixon. You have a lot of good days. That was just one of many that you cite, that occasion in Chicago.

As a member of the Finance Committee, we are tied up on the floor today with an issue of some consequence which carries over from yesterday, so I cannot remain for long today because of my involvement there. But I want to make an opening statement myself because of the importance I attach to these hearings and how much I appreciate the strong start that you have made, Senator Dixon, with respect to the work of this subcommittee with the help of Senator Bond.

Last year when we reviewed a number of these issues in the context of the Proxmire Financial Modernization Act of 1988, it became very clear that it would be difficult to enact legislation providing banks additional powers unless there had been some resolution of the subjects which are the topic of these hearings. I think the same is true today.

Legislation dealing with government check cashing and Community Reinvestment Act improvements have now been before this committee for as long as plans to further modernize the financial services industry. I think both matters deserve our equally serious consideration and I think we need to move on both.

I believe that last year the committee came sufficiently close to reaching agreement on the government check cashing and Community Reinvestment Act issues and that legislation in these areas is now clearly something we can accomplish.

More work probably needs to be done regarding the lifeline checking issues.

Mr. Chairman, you have a well-deserved reputation of being a master at bringing together divergent viewpoints and producing a consensus and this committee has seen that on a number of occasions. The three issues you are tackling in these hearings—government check cashing, lifeline checking, and Community Reinvestment Act improvements—have proven to be highly contentious over the years with consumer groups on the one side and the bankers on the other.

I believe in the past that there has been some give on both sides and more is probably needed, but under your very able leadership, Senator Dixon, and that of Senator Bond, together with the rest of the subcommittee, I believe that we can see a resolution of a number of the remaining issues and I think our goal should be to pass legislation in this Congress in these areas.

So as soon as you are able to reach agreement on any or all of these issues, I am prepared to take them up for markup at the full committee level and move these things forward on to the Senate floor and into law.

Finally, let me commend you also, Chairman Dixon, for your choice of witnesses this morning. You've assembled an outstanding group of witnesses to testify and I especially want to welcome two Michigan constituents, one who has already testified—that is, of course, Board Member Martha Seger, and I am reviewing her testimony now, and later we will hear from Charles Conville who is the President and CEO of PrimeBank, a Federal savings bank of Grand Rapids, MI. We're delighted that he is here as well.

So, let me again say how strongly I support the work you are doing and the vigorous start you've made.

Senator DIXON. Well, Mr. Chairman, let me say on behalf of the ranking member and myself, we feel very honored to have you here first and also to have your expression of support as chairman of the whole committee indicating, as I had hoped you would, that whatever result we obtain in this subcommittee will be considered for markup by the whole committee. That is a great step forward for us and I appreciate it very much. I appreciate your usual good attention to all the detail in the committee.

Senator RIEGLE. Thank you.

Senator DIXON. Thank you, Mr. Chairman.

Mr. Clement, we are delighted to have you here and I know my friend from Missouri is always pleased to see distinguished representatives of the business community in St. Louis here. We're pleased to have you, Mr. Clement.

STATEMENT OF CHARLES F. CLEMENT, SENIOR VICE PRESIDENT, LANDMARK BANK, ST. LOUIS, MO

Mr. CLEMENT. Thank you very much, Mr. Chairman.

Landmark Bank has been working closely with the Missouri Association of Community Organizations for Reform Now, more commonly known as ACORN, since 1986. During this time we've been successful in establishing a home improvement loan program specifically targeted to low and moderate income borrowers in the city of St. Louis and St. Louis County.

As the bank's senior vice president responsible for consumer real estate lending, it has been my task to ensure that our lending officers are fully aware of the bank's obligations under the Community Reinvestment Act and that they understand Landmark's loan policies and programs as they relate to low and moderate income applicants.

DISCOUNTED LOANS

In an effort to make home improvement loans more affordable to low income applicants, we have discounted these loans at 4 percentage points below the rate generally offered. Today's standard rate on home improvment loans, for instance, is 13½ percent. Our below market loans are available at the rate of 9½ percent. This discounted rate lowers the monthly loan payments and enables more applicants to qualify for a more affordable loan.

Additionally, we have broadened our normal loan underwriting guidelines in an effort to make these loans available to more applicants. We nevertheless expect all loans to be repaid as agreed and an applicant's past credit and employment history are weighed heavily in arriving at a final credit decision.

As part of our arrangement with ACORN, Landmark Bank sponsors periodic seminars on home improvement and home purchase loans. Additionally, since the first quarter of this year, a Landmark Bank loan officer has been meeting with prospective applicants at ACORN's offices on a monthly basis. These conferences are held from 5:30 p.m. to 9:30 p.m. so that applicants who cannot get away from their workplace during the day have an opportunity to meet with a banking representative after normal banking hours to discuss their personal borrowing needs.

Senator DIXON. That's terrific.

Mr. CLEMENT. A number of successful loan situations have resulted from these after-hour loan conferences and I would like to discuss two of them with you this morning.

Several years ago, the city of St. Louis, along with the Department of Housing and Urban Development, instituted a homesteading program whereby families who did not have the means to purchase a home could live in a dwelling owned by HUD. After living in the home for a period of at least 3 years and making certain required repairs to the home, the family would receive the deed to the property.

Earlier this year, HUD and the agency handling this homesteading program for the city issued a deadline to the families who had not yet completed the repairs necessary to transfer ownership of these homes. A member of ACORN staff in St. Louis, Miss Justine Petersen, learned of three of these situations and contacted me to determine whether Landmark could help these people.

Because these individuals did not have title to the real estate and were therefore in no position to offer a lending institution a valid lien on the residence as collateral for a home improvement loan, most lenders were unwilling to consider a loan request from the applicants. I was happy to meet with the individuals to discuss how Landmark might be able to assist them with their special needs.

In each situation, less than $7,000 was required to complete the improvements needed to qualify the home for transfer of ownership. After meeting with each of the borrowers and making a personal inspection of the properties in question, we were able to grant approval to two of the applicants.

The process that ensued involved working with the borrower, the contractor, a title company, and the Community Development

Agency of the city of St. Louis, to arrange to have the improvements completed to the satisfaction of the CDA and HUD so that title to the property could be transferred to the borrower simultaneously with the disbursement of the loan proceeds to the contractor. This entailed convincing the contractor to accept the bank's commitment to fund the cost of all repair work only upon satisfactory completion and in lieu of the customary downpayment from the borrower.

By working out these details, Landmark Bank has two new loan customers with both loans being well secured by first mortgages on the properties, and the city of St. Louis has two new home owners.

While the total dollars involved in these two transactions are small in absolute numbers, the importance to the borrowers of the availability of these funds is immeasurable.

I could tell you about other home improvement and home purchase loan situations that have evolved from Landmark Bank's involvement with ACORN and other community groups, but unfortunately, my allotted time does not permit it.

Let me conclude by saying that we envision Landmark's commitment to its compliance with the Community Reinvestment Act as an ongoing bank policy, including active participation with neighborhood groups, organizations and individuals throughout our lending area.

I want to thank you for inviting me here this morning to share these success stories with you.

[The complete prepared statement of Charles F. Clement follows:]

Landmark Bank
Member FDIC

SUMMARY

Testimony of
Charles F. Clement
Senior Vice President
Landmark Bank
St. Louis, Missouri

before the Subcommittee on Consumer and Regulatory Affairs
Senate Banking Committee
Wednesday, June 7, 1989

- Landmark Bank has been working with ACORN since 1986.
- Below-market home improvement loans are available to low- and moderate-income applicants.
- Landmark's underwriting guidelines for such applicants have been broadened to increase loan opportunity.
- A Landmark Bank consumer loan officer meets monthly with applicants at ACORN's offices after normal banking hours to facilitate the applicants ability to meet with a bank loan officer.
- Two applicants have acquired title to homes available through the City of St. Louis "Homesteading" program using below-market home improvement loans from Landmark Bank.
- Landmark's commitment to its compliance with the Community Reinvestment Act is an ongoing program throughout the communities that Landmark serves and includes involvement with many community organizations, in addition to ACORN.

LANDMARK BANK
Community Reinvestment Program

Landmark Bank has been working closely with the Missouri Association of Community Organizations for Reform Now (ACORN) since 1986. During this time we have been successful in establishing a home improvement loan program specifically targeted to low- and moderate-income borrowers in the City of St. Louis and St. Louis County. As the bank's senior vice president responsible for consumer real estate lending, it has been my task to ensure that our lending officers are fully aware of the bank's obligations under CRA, and that they understand Landmark's loan policies and programs as the relate to low- and moderate-income applicants.

In an effort to make home improvement loans more affordable to low-income applicants, we have discounted these loans at four percentage points below the standard rate offered on our home improvement loans. (Today's standard rate on home improvement loans is 13.5%; our below-market loans are available at a rate of 9.5%.) This discounted rate lowers the monthly loan payments and enables more applicants to qualify for a more affordable loan. Additionally, we have broadened our normal loan underwriting guidelines in an effort to make these loans available to more applicants and are more flexible in our loan underwriting. We nevertheless expect all loans to be repaid as agreed, and an applicant's past credit and employment history are weighed heavily in arriving at a final credit decision.

As part of our arrangement with ACORN, Landmark Bank sponsors periodic seminars on home improvement and home purchase loans. Additionally, since the first quarter of this year, a Landmark Bank loan officer has been meeting with prospective applicants at ACORN's offices on a monthly basis. These conferences are held from 5:30 p.m. to 9:30 p.m. so that applicants who cannot get away from their workplace during the day have an opportunity to meet with a banking representative after normal banking hours to discuss their personal borrowing needs. A number of successful loan situations have resulted from these after-hour loan conferences, and I would like to discuss two of them with you today.

Several years ago, the City of St. Louis, along with the Department of Housing and Urban Development, instituted a "Homesteading" program whereby families who did not have the means to purchase a home could live in a dwelling owned by HUD. After living in the home for a period of at least three years and making required repairs to the home, the family would receive the deed to the property. Earlier this year HUD and the agency handling this "Homesteading" program for the City of St. Louis issued a deadline to the families who had not completed the repairs necessary to transfer ownership of these homes. A member of ACORN's staff in St. Louis, Ms. Justine Petersen, learned of three of these situations and contacted me to determine whether Landmark could help these people. Because these individuals did not have title to the real estate and were therefore in no position to offer a lending institution a valid lien on the residence as collateral for a home improvement loan, most lenders were unwilling to consider a loan request from the applicants. I was happy to meet with the individuals to discuss how Landmark could help them with their special needs.

LANDMARK BANK
Community Reinvestment Program (cont'd.)

In each situation, less than $7,000 was required to complete the improvements needed to qualify the homes for transfer of ownership. After meeting with each of the borrowers and making a personal inspection of the properties in question, Landmark was able to grant approval to two of the three applicants.

The process that ensued involved working with the borrower, the contractor, a title company and the Community Development Agency of the City of St. Louis, to arrange to have the improvements completed to the satisfaction of the CDA and HUD so that title to the property could be transferred to the borrower simultaneously with the disbursement of the loan proceeds to the contractor. This entailed convincing the contractor to accept the bank's commitment to fund the cost of all repair work upon satisfactory completion, in lieu of a customary downpayment from the borrower. By working out these details, Landmark Bank has two new loan customers, with both loans well-secured by first mortgages on the properties, and the City of St. Louis has two new homeowners. While the total dollars involved in these two transactions are small in absolute numbers, the importance to the borrowers of the availability of these funds is immeasurable.

I could tell you about other home improvement loan situations that have evolved from Landmark Bank's involvement with ACORN and other community groups, but unfortunately, my alloted time does not permit it.

Let me conclude by saying that we envision Landmark's commitment to its compliance with the Community Reinvestment Act as an ongoing bank policy, including active participation with neighborhood groups, organizations and individuals throughout the St. Louis area.

Thank you for inviting me here this morning to share these success stories with you.

6/7/89

Senator DIXON. Well, I just want to say, Mr. Conville, in the allotted time you did a splendid job. I wish everybody in America could hear the story of what the private sector making a decent profit can do when it tries to work with the community groups to help the neighborhoods. I just feel real good about your story.

Ms. Cunningham, I come from Bellville across the river. Your good name and your good reputation and the good work you do is well known to this Senator and we're delighted to have a representative of ACORN here. You've done great work in the communities around the country and we're interested in hearing your testimony.

STATEMENT OF MARY ANN CUNNINGHAM, REPRESENTING THE ASSOCIATION OF COMMUNITY ORGANIZATIONS FOR REFORM NOW

Ms. CUNNINGHAM. Thank you, Senator Dixon.

Senator Dixon, Senator Bond, and members of the subcommittee, I am Mary Ann Cunningham. I chair the Banking Committee of ACORN and I'd like to share a few things with you this morning concerning our successes in St. Louis.

St. Louis ACORN has made progress and is experiencing success with some of the banks under CRA. We've used CRA as a much needed mechanism that is being used to upgrade our community. Under CRA, we are seeing low and moderate income residents who are, for the first time, being given the opportunity to purchase homes and to maintain them and make necessary repairs.

While this is good for the individual, it is an enhancement to our community. St. Louis has so many delapidated and abandoned homes that have been purchased by low-income and moderate-income residents, and this was possible through CRA. They have rehabilitated these homes and they are very responsible home owners. Without CRA, some of this would not have been possible.

We can also tell you of other interesting things under CRA that have happened through banks such as the Landmark Bank and Boatmen's Bank. We meet with them quarterly to discuss statistical data that we have gathered and that the bankers have compiled to show the actual number of the loans that have been applied for and the number that have either been granted or denied and the reasons for such denial.

These statistics are tracked by census tracks where the loan applicants do reside. This gives us a good view of the progress being made. In areas where improvement is needed, we make recommendations on ways in which these programs can be improved with the banks and where more emphasis is needed to help the low and moderate income segments of the community.

The problems we are experiencing are because the provisions of CRA are not being met. The 12 assessment factors are not being complied with and results of Federal examinations are not disclosed to the public. As we know, CRA does require that banks do meet the needs of the community. However, the examiners from the four Federal agencies when they rate the banks, the ratings are private. Therefore, the public is not informed of these ratings.

They are not aware of the areas where they should be eligible for financial assistance.

Therefore, the needs of the low and moderate income people are not being met.

With public disclosure of the ratings, community organizations would have more latitude to work with those that are not in compliance with the legal obligations under CRA. We could encourage incentives for those who do participate in this sociably responsible investment movement. We could encourage organizations, such as churches and labor unions, to do business with them. As it is, we're doing business with those who are actually defying our community's needs.

If we had access to examination ratings, the exams would have greater meaning and the performance by the banks probably would be better.

We would like to see them improve so that they would better meet the needs of the low and moderate income segments of the community.

It would allow community organizations to target their energies to the areas where it is needed. Disclosure of these examinations actually are discriminatory practices, such as red lining. With disclosure of these examinations, it might even help our minority entrepreneurs who do find that they meet with very indifferent attitudes from the bankers. Most bankers resist CRA because it allows community organizations to protest applications for opening or moving a facility when the legal obligations are not being met under CRA. They don't like the community to have the right to challenge them.

Since the Federal Reserve Bank cannot approve challenged applications until circumstances surrounding the challenges are resolved, we are getting resistance from these bankers.

I thank you very much, Mr. Chairman, for this time. Thank you for inviting me to testify this morning.

[The complete prepared statement of Mary Ann Cunningham follows:]

Testimony presented to the

Subcommittee on Consumer and Regulatory Affairs
Committee on Banking, Housing and Urban Affairs
US Senate
Senator Alan Dixon, Chair

by
Mary Ann Cunningham
representing
ACORN
The Association of Community Organizations for Reform Now

June 7, 1989

ACORN is grateful to Chairman Dixon and other Members of the Subcommittee on Consumer and Regulatory Affairs for inviting us to testify at these hearings.

ACORN strongly supports efforts to add protections and reforms to the S&L bailout bill. We specifically endorse that legislation to mandate CRA exam disclosure, to expand the Home Mortgage Disclosure Act, and to require banks to offer low cost checking accounts and cash government checks for nonaccount holders. These reforms are vital and integral to the S&L bailout legislation. We urge that these measures be adopted by the Senate (if they are among the options) in conference. Legislation to accomplish these purposes has been introduced by Senator Howard Metzenbaum: S. 906, S. 907, S. 908 and S. 909. Simillar bills are moving through the House of Representatives under the sponsorship of Congressmen Kennedy and Gonzalez.

ACORN

•ACORN, the Association of Community Organization for Reform Now, is the country's largest organization of low and moderate income people. Founded in Arkansas in 1970 by a group of welfare mothers, ACORN has grown to include 80,000 member families in 26 states. ACORN groups are first organized at the neighborhood level to work for neighborhood improvements. As a national organization, ACORN is governed by an Association Board, composed of two delegates elected from each state. The Association Board is responsible for the overall direction of ACORN, for national campaigns and policy decisions.

•ACORN is a multi-issue, multi-racial organization. Every day, ACORN members work through neighborhood groups to win improvements in our local communities, and also come together through citywide and national campaigns to tackle larger, common problems. ACORN members address a range of issues including expanding and preserving the stock of low income housing; fighting rape; providing jobs for the long-term unemployed; removing barriers to voter registration; and improving education, health care, and police protection.

•Since 1985 ACORN has been fighting to force banks to improve their lending in our neighborhoods. ACORN has met with officers of more than 40 banks concerning bank compliance with the Community Reinvestment Act (CRA) and as an outcome, has negotiated 25 CRA agreements in which lenders have agreed to make more than one-half billion dollars available on special terms in low and moderate income neighborhoods over the next two years. ACORN is also fighting to push reforms of CRA and related laws through Congress. ACORN's involvement in the savings and loan bailout issue is a direct outgrowth of our banking campaign.

CRA exam disclosure

There is a clear need for legislation to require the banking regulatory agencies to publicly disclose their reports of bank and thrift compliance with the Community Reinvestment Act.

•The Community Reinvestment Act is not being enforced. The evidence of lack of enforcement of CRA is so ample and pervasive that it seems we have lost the ability to see the forest or the trees.

In the last year, major metropolitan newspapers, including the Atlanta Journal-Constitution, The Detroit Free Press and the Boston Globe have reported extensively on racial discrimination in lending in their communities. The Atlanta Journal-Constitution series, "The Race for Money" was compelling enough to win its principle author, Bill Dedman , a Pulitzer prize and to put 64 depository institutions in the Atlanta area under investigation by the US Department of Justice for violation of civil rights laws.

There is a different kind of evidence of lack of CRA enforcement with which no reasonable person can take issue. Credit is the lifeblood of communities. As we survey the country, we see it spattered with slums. There are neighborhoods within a few block of where we are sitting, and in every state and city and rural community in this nation, crumbling as a consequence of redlining and financial disinvestment by private lenders and governments. The lives of people in these disinvested areas are, for the most part, shorter and bleaker than for the rest of Americans.

That's the plain truth about CRA enforcement. Federally regulated depository institutions --including 15,000 commercial banks and 3,000 savings and loans--have an affirmative obligation to meet the credit needs of low and moderate income people within their service areas. Many of these institutions are not meeting this obligation. If these institutions were living up to their duties, the ghetto would bloom.

•Among the many reasons that CRA is not being enforced is that bank examiners have little inducement to perform probing and comprehensive exams into bank compliance with CRA. And assuming that the exceptional examiner were to perform a high quality exam, and discover that a bank is breaking this law, there is no apparent commitment at the top of the agencies to impose though sanctions against violators.

ACORN believes that a significant improvement in this situation could be achieved if Congress required the regulatory agencies to make public the detailed examination reports of bank compliance with CRA. Such disclosure would create an incentive for regulators to produce a high quality work product. It is quite natural to treat a task as a formality, to give it a cursory lick and a promise, when one knows that it will never receive broad scrutiny. When concerned citizens can check their perceptions of a bank's lending record against the evaluations produced by examiners, examiners may feel strongly motivated to take this part of their job more seriously.

• Disclosure of CRA exams may result in improved bank performance. When bankers can shroud their policies and practices in mystery and double talk, it is hard for average people to hold them accountable. If the public had detailed information about what efforts a bank or savings and loan was making to meet the credit needs of low and moderate income neighborhoods, the officers and stockholders of these institutions would be identified with their behavior. Knowing that one is being watched can be a powerful stimulus to live up to one's responsibilities.

• If bank compliance improved, in part as a consequence of CRA exam disclosure, community groups would not need to file as many CRA challenges. ACORN is well aware that CRA challenges are disliked all around -- by bankers, regulators and community groups. There is no need to elaborate on why bankers and regulators are not fond of CRA challenges, but it may be in order to explain what an exhausting, gritty and miserable task it is to bring a CRA challenge. The hard work begins with community leaders getting other members of the community up-to-speed on their rights under CRA, and other relevant details about the law and the financial services industry. Banking is fairly mysterious to almost everyone but it lies far from the daily experience of most poor people. The clock on the comment period is ticking. People work long into the evening, after a full day at a paid job, gathering information, checking and double checking its accuracy, and writing up the narrative. Face to face negotiations with banks, which can be quite intimidating for outsiders like ACORN members, can go on night after night. There is no guarantee of success and there is little recourse if bankers and regulators decide to stonewall us.

• Although community groups dislike CRA protests even more than bankers do, it is crucial to stress that ACORN, and allied groups around the country are prepared to fight as hard and as long as necessary to protect our legal right to file CRA challenges, and to prevent further weakening of our standing in this process. It is apparent that our right to claim that a bank's application for expansion should be denied because that bank is not in compliance with the Community Reinvestment Act is, at present, one of the few tools we have to prompt banks to pay attention to low and moderate income people and our need for credit and deposit services.

ACORN is not limited to doing challenges --we picket, sit in bank lobbies, and use other forms of direct action. ACORN could even mount an extended campaign against a major bank. But CRA challenges are the most effective weapon community groups have against redlining.

•As a consequence of our unshakable support for public participation in the application process, we must strongly oppose Section 703 of the CRA amendment to HR 176. This section would give us, perhaps, an opportunity to participate more fully in the the CRA exams performed by regulators. We support active citizen participation in all of the vital institutions in our society, especially the financial services industry. We do hope, as the banking committees of local ACORN groups mature, that we can keep better tabs on our banks and S&Ls on an ongoing basis.

But it is wholly unrealistic to expect that low and moderate income people are ready, willing and able to play a major part in every routine CRA exam of every bank. We have attached copies of eight pages of the St. Louis phone book to our testimony to graphically illustrate the very large number of depository institutions in even a medium sized city like St. Louis. ACORN members simply do not have time to become volunteer bank examiners. We hope that the large and able band of people on the examination staffs of the four bank regulatory agencies really are looking out for our welfare, are genuinely becoming sensitized to matters of class and race, and will dramatically improve the enforcement of the Community Reinvestment Act.

•ACORN urges Congress, in short, not to fix CRA -- because it is not broken. As our stories from St. Louis and around the country show, agreements reached between banks and community groups get essential credit into disinvested neighborhoods and make a profit for banks. We encourage Congress to put a little oil in the system by mandating disclosure of CRA exam reports, but no major overhauls, please!

• If community groups had access to CRA exam reports, we could get a much clearer picture of which are the good, the bad and the indifferent banks. We could target our energies to put pressure on the poor performers and provide a variety of rewards to good corporate citizens. There are many individuals and organizations interested in socially responsible investing -- in working with banks and other financial institutions who care about the consequences of their policies for the quality of life in this country. CRA exam disclosure would help identify these investment prospects.

As matters stand, when a community group is deciding whether or not to bring a CRA challenge against a bank application, we must piece together information that is often spotty and anecdotal. Aside from HMDA (Home Mortgage Disclosure Act) data there is no way for low and moderate income groups to get a comprehensive picture of lending practices. CRA disclosure is in the clear interest of banks willing to obey the law.

•CRA agreements need to be monitored for the life of the agreements. Access to exam data would be extremely useful, for both banks and community groups, in determining whether banks are fulfilling the terms of their agreements.

ACORN believes that disclosure of CRA exams would result in better exams, better bank performance, fewer protests, --- and fewer dying neighborhoods. We strongly urge passage of disclosure legislation.

Successes in St. Louis

St. Louis is a city with serious housing problems. ACORN members realized that it was very hard to get a loan from a bank, that like so many other cities St. Louis was systematically redlined. Members were angry -- they could see their neighborhoods steadily deteriorating and the regulators turning their backs. We had many abandoned homes in our neighborhoods and many families living in inadequate rental housing who should have been able to own their own homes. ACORN set about developing some solid proposals to turn this problem around, a strategy for challenging the merger of the largest bank in the state and the oldest bank west of the Mississippi -- Boatman's.

Boatman's Bank, owned by the state's largest bank holding company made no home mortgage loans in 1982 and 1983, and when the bank did begin making mortgage loans in 1984, only 8% were made in the City of St. Louis, with the remainder being made in more affluent St. Louis County. Furthermore, during those same years the bank made only between 7% and 13% of its home improvement loans in census tracts where housing values were below the St. Louis median.

ACORN invested tremendous amount of resources in this challenge. Members tried to assess what credit and deposit needs weren't being met in our communities. They researched the bank's policies as extensively as they could over a two month period. As nearly as possible ACORN members tried to get information on all the CRA assessment factors and to take the analysis of bank's record very seriously. Members studies HMDA data for a three year period and analyzed the census tracts where the loans were made. The East-West Gateway provided additional information about the demographic characteristics of these census tracts. Members collected information on where the bank said it was putting its money. They found that the bank was financing some rental units and checked on the average rent for the units to see if it was a gentrifying project. Members looked into the locations of branch banks, studied advertising, assessed overall service, including special services like government check cashing for people without accounts. ACORN sent members into the bank to see what the employees told them, and later members checked on this information over the phone. ACORN contacted some of the groups the bank said they worked with to see what they were really doing. Many groups were barely operating. Other were just getting a contribution which did nothing to expand and improve low and moderate income housing.

In preliminary discussions officers of Boatman's stated that their record for CRA compliance had never been questioned. ACORN's accusations, therefore, caught Boatman's off-guard. Given what ACORN had uncovered about this bank's lending record, we had to question what kind of CRA ratings they had been getting. Employees at Boatman's hinted that they had a good rating, a very favorable rating.

As an outcome of all of this, when General Bancshares Corp. applied to acquire Boatman's Bankshares, Inc. ACORN challenged that application on CRA grounds and won a commitment from Boatman's to invest $50 million a year in low income housing in St. Louis. Among other provisions, the signed agreement between ACORN and Boatman's set up a joint ACORN-bank review committee to assess the progress of the drawdown of the money. We have included a copy of our CRA agreements with Boatman's and Landmark, as well as a report prepared by Boatman's on their progress in meeting the terms of the agreement. John L. White, Senior Vice President of Boatman's, states in the cover letter to the progress report that by February 23, 1989, the bank had exceeded "exceeded our original lending goal of $50 million by more than twice -nearly $103 million."

Ethan A.H. Shepley, Jr., vice chairman of Boatman's, speaks very favorably of the agreement his bank reached with ACORN, stating that the results of such agreements can be good for a bank. "We're being held up as the heroes, and that's super. That's the kind of publicity we love. And we've not making any loans that we feel are bad".

Missouri ACORN has negotiated four major Community Reinvestment Act agreements--with Boatman's, South Side National, Landmark, Mark Twain banks--plus another ten agreements which deal specifically with lifeline deposit accounts.

Lifeline accounts developed after negotiations with Missouri ACORN are bringing thousands of new customers through bank doors. Charles E. Silva, Jr. Executive Vice President of Landmark Bank reports that his bank opened 2,000 "Pay As You Go" accounts last year, bringing the total of lifeline customers to 7,000. And Merchantile Bank had 2,675 "Budget Checking Accounts" as of Sept. 1987.

ACORN has developed a very productive and favorable relationship with Landmark. The bank has been very willing to accept ACORN and seek out our input. A loan officer from Landmark comes to the ACORN office one day a month to process loan applications after ACORN has done prescreening. ACORN flyers the neighborhoods, contacts the churches, spreads the word about the loan campaign.

Landmark has had the best success in St. Louis with their lifeline accounts; they offer 4% below market rate for home improvement loans -- with up to ten year terms. And Landmark has the only bank in Wellston, the poorest suburb in the area.

Mark Twain Bank deserves recognition also. The bank has worked to develop a voluntary association of banks to offer uniform lifeline accounts. These banks would display a logo to identify themselves as concerned and involved corporate citizens.

In short, CRA can work. With help from Congress and the regulators CRA could be a fulcrum for turning around the most severe problems faced by low and moderate income communities in America.

LANDMARK BANK/ACORN PROGRAM
September 9, 1986

1. Landmark Bank has no plans to close any banking offices, and is engaged in a program to open a number of retail locations in the St. Louis market.

2. Landmark offers "lifeline" services, and these include/will include the following characteristics:

Pay As You Go Checking

Opening Balance:	$25
Minimum Balance:	None
Regular Fees:	Free if average monthly balance is $100 or above. $1 per month charge if average monthly balance falls below $100. 15c for each check. No charge for access through automated teller machine.
Non-sufficient Funds:	$5 per bounced check until such time as an accountholder has three NSF checks in a calendar quarter or six NSF checks in a calendar year, at which time the NSF charge will be $15 thereafter.

Savings

Opening Balance:	$25
Minimum Balance:	None
Regular Fees:	Free if average quarterly balance is $100 or above. $5 per quarter charge if average quarterly balance is below $100. Six withdrawals per quarter without charge. $1 for each withdrawal over six per quarter. No charge for access through automated teller machine.
Money Orders	$1 per money order regardless of amount of money order.

Government Checks

Landmark cashes government checks of any amount and at no charge for Landmark customers.

On a six-month trial basis, Landmark will cash government checks for non-customers at any Landmark Center in the City of St. Louis or St. Louis County, strictly according to the following guidelines:

- The check must be issued by the U.S. government or by a recognized, solvent state or municipal body.
- The check must be in an amount of not more than $400.
- The check must be endorsed by the payee.
- The check may only be cashed in person, by the payee.
- The payee must present two pieces of valid identification, including a valid drivers license or state identification card, and may be asked to endorse the check in the presence of a Bank officer.
- A fee of $3.00 per check will be charged for each check cashed.

Landmark will review this policy six months after it takes effect to determine losses, operational difficulties or customer relations problems resulting from the policy. At that time any adjustments may be made, including suspension of the policy.

Landmark notes that these services are comparable to or more favorable than other "lifeline" services in our market area.

3. Landmark will commit annually up to $6.5 million for loans targeted to low-to-moderate income applicants, low-income neighborhoods and low-to-moderate income and first-time business people. The loan pool breakout will be:

$3,000,000	Home Purchase Loans
$1,500,000	Small Business Administration Loans
$1,500,000	Commercial Loans
$ 500,000	FHA Home Improvement Loans at 4% below market

In an effort to distribute these loans to the greatest number of qualified applicants, Landmark will place reasonable restrictions on the total dollar amount it will lend to any one applicant.

Landmark maintains flexible underwriting criteria for all lending categories. Credit worthiness and ability to repay are primary considerations. When evaluating loan applications, Landmark considers, without bias: total household income -- including public assistance, food stamps and income from other governmental sources; income from self-employment and part-time employment; verifiable cash income, as well as continuity of income.

Loan applicants' total monthly debt ratios should not exceed the least restrictive federal guidelines. However, if the applicant demonstrates the ability to meet these higher loan payments, the Bank will waive such guidelines.

Landmark's lending policy cites,

"Management believes that sound loans within the markets we serve are the most desirable means of employing Bank funds for lending. Therefore, we will aggressively seek to develop markets for credit to the fullest extent possible. . . . Sound loans are defined as those which: make economic sense for this Bank; have reasonable certainty of repayment; or, with the concurrence of Bancshares, the Board of Directors and the management of the Bank have social or community significance which would not otherwise be acceptable under credit policy. . . . It is the policy of the Bank to fully comply with all state and federal laws and regulations relating to the extension of credit. The Board of Directors, the Management and the loan officers are responsible for assuring compliance with such laws and regulations that now exist or hereafter may be enacted. Without limiting the general policy of full compliance, the Bank specifically recognizes its obligations under the following laws and regulations.

Equal Credit Opportunity (Regulation B). The Bank will not discriminate on the basis of race, religion, sex, national origin or marital status with respect to any credit transaction, including applications for credit and extension of credit. The Bank recognizes that inquiries concerning marital status, spouse or former spouse, alimony and child support income and childbearing intentions are strictly regulated by Regulation B. . . . Community Reinvestment Act. The Bank will accept for processing any credit application regardless of the geographic location of the applicant or collateral property. The Bank is committed to helping meet the credit needs of low and moderate income areas. The Bank will not condone any red-lining or reverse red-lining practices...."

5. Landmark directors, seven senior bank officers, and 10 advisory directors who represent businesses and communities in the metropolitan St. Louis area, will review community-related programs and services at regularly scheduled meetings.

   Landmark will maintain quarterly written reports of its board of directors' review of community-related programs, and will provide copies of the reports to ACORN on an ongoing basis and to other community organizations and the general public upon request.

   Landmark's quarterly board review and written report on community-related programs will discuss 1) loan applications submitted, 2) loans funded, 3) loans not funded and 4) the reasons why loans were not funded, for the loans included in this Program.

   Landmark officers are and will be available for consultations and periodic meetings with community and neighborhood service and business organizations.

6. Landmark has made lines of credit loans, and will continue offering lines of credit, to credit unions serving the greater St. Louis metropolitan area, consistent with good credit practices and the merits of the applications.

7. Landmark maintains hiring practices consistent with state and federal laws and solicits and welcomes applications for employment by individuals and recommendations of individuals for employment by ACORN or other responsible community organizations. Landmark will make every reasonable effort, consistent with state and federal law, to send written notification to ACORN of job openings as they are posted and advertised.

8. Landmark will donate foreclosed housing to responsible not-for-profit housing development organizations when and if such donation is consistent with Landmark's fiduciary, legal and regulatory obligations and responsibilities. Landmark will make every reasonable effort to send written notification to ACORN of such opportunities as they arise.

9. Landmark will waive or modify fees for accounts, loans and services to responsible, not-for-profit housing development corporations whenever such waivers or modifications are possible, consistent with enlightened corporate citizenship and good business practices. Landmark will make every reasonable effort to send written notification to ACORN of such actions as they arise.

10. In marketing its "lifeline" banking services, special credit programs and flexible credit evaluation policy, Landmark will:

- Publish and display brochures describing Landmark's Pay As You Go checking and Community Reinvestment Program;
- Provide ample supplies of brochures to ACORN and to other responsible community organizations, political and neighborhood groups, upon request, for distribution to individuals in the communities they serve;
- Build a 1987 advertising program using media which targets predominantly low-to-moderate income geographic areas and audiences;
- Continue to be responsive to recognized community organizations who periodically request involvement in or support of business fairs, seminars, outreach programs, publications and other effective means of communicating the uses and availablity of financial services for low-and-moderate income individuals and businesses.
- Landmark has committed $10,000 to be distributed to responsible community organizations, selected by Landmark, to be employed in programs which enhance responsible use of financial services by low-to-moderate income individuals.

For Landmark Bank Gerald W. Schoor
Gerald W. Schoor, Chairman of the Board

For Missouri ACORN Carl Toledo
Carl Toledo, Chairman of the Banking Committee

September 10, 1986

THE BOATMEN'S
NATIONAL BANK
OF ST. LOUIS

THE BOATMEN'S TOWER
100 North Broadway, Box 236
St. Louis, Missouri 63166
314 425-7500

ETHAN A. H. SHEPLEY, JR.
Vice Chairman of the Board
314 425-7913

November 14, 1985

Missouri Association of Community
Organization for Reform Now
4144 Lindell Boulevard
St. Louis, Missouri 63108

To The Members of Acorn:

The Boatmen's National Bank of St. Louis has a long and proud history of working with the community in making St. Louis a better place to live and work. Historically, we have provided help to improve the quality of life in our community.

In this context and with the impending merger of eight Boatmen's Banks in St. Louis and St. Louis County, into The Boatmen's National Bank of St. Louis, we are happy to announce that we will consolidate the various low and moderate income loan programs which are in place at each individual bank. The best of these programs will be formalized into a new Community Reinvestment Program which will be augmented by an overall commitment by the Bank to make available up to $50 million in low to moderate income housing areas and by grants totalling $100,000 annually to neighborhood organizations to help promote and assist the Bank in the loan packaging.

The new Community Reinvestment Program will incorporate the following features:

1. THE LENDING PROGRAM

The Bank will make a reasonable effort, within the bounds of prudent banking practice, to make available $50 million in loans to low to moderate income areas in greater St. Louis during 1986 and beyond. The majority of these loans will be housing-related.

The Bank will make housing-related loans including permanent mortgage financing for purchase and rehabilitation of one to four family residences, for purchase and rehabilitation of multi-family residential buildings, short-term loans for construction or rehabilitation on projects qualifying for permanent financing under the program and home improvement rehabilitation loans on single family (one to four), owner-occupied structures. Loan funds will be allocated solely on the basis of need and regardless of loan category.

Loan terms and pricing will be in the province of the Bank which will exercise a high degree of flexibility in meeting loan requests. As an inducement to help the Program get started and

as a show of good faith, the Bank will make the first $500,000 in loans at 2% below the then market rate. In addition, the Bank will endeavor to make additional favorable pricing in the Program by seeking government and other alternative sources such as grants, loan guarantees or interest write-downs.

The Bank will waive application fees for not-for-profit developers of housing in the qualifying areas.

The Bank will make every effort to process all loan applications as quickly as possible.

2. THE LOAN GUIDELINES

The Bank recognizes that there are no standard loan guidelines for low to moderate income borrowers. Maximum flexibility will be used on a case by case basis when these loans are being considered. Credit-worthiness is the major consideration and shall be determined by taking into account the entire family income, including public assistance, self-employment and part-time employment.

Loan applicants must demostrate an ability to maintain income continuity over time, regardless of the variety of employers.

Credit history of prompt payment is important, but will not necessarily be required of all applicants. Each applicant's credit record will be judged on a case by case basis.

Loan applicants' total monthly debt ratios should not exceed the least restrictive Federal guidelines. However, if it can be demonstrated that the applicant has the ability to meet these higher loan payments, the Bank will waive such guidelines.

The Bank recognizes the value of "sweat equity" on a case by case basis and will consider it the equivalent of a cash investment in rehabilitated property. The Bank will lend as high as 95% of the appraised value of the property on a case by case basis.

Under proper circumstances, the Bank will extend time periods for completion of rehabilitation projects by not-for-profit developers and the Bank will make loans on a non-recourse basis

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to not-for-profit developers whose expertise qualifies them as capable rehabilitators.

All appraisers used by the Bank in evaluating property for housing-related loans shall be persons with experience in appraising low to moderate income properties.

3. NEIGHBORHOOD GRANT

The Bank recognizes the value of having trained neighborhood loan packagers in the targeted neighborhoods and intends to grant the sum of $100,000 annually to help subsidize the training and salaries of a packager from each neighborhood group awarded a grant. No grantee shall receive more than $10,000 annually. It is the Bank's intention to encourage as many neighborhood organizations as possible to enlist in the Program. The Bank will furnish officers to inform interested groups about the Program, to explain the application forms involved with each of the various loans, and the procedures to follow for submission and possible approval.

4. BANKING SERVICES

The Bank recognizes the importance of a banking service to persons of low to moderate incomes and with the following features:

- a. Minimum deposit - $25.00
- b. 200 checks for $5.20
- c. Monthly maintenance charge - $2.50
- d. 5 free checks monthly - each check over 5 @ 50c
- e. Returned checks - $5.00 per item
- f. Free "Option 24" card to obtain cash from over 30 automatic teller machines in greater St. Louis. No charge for machine transactions.
- g. No need for money orders with the Economy Account.
- h. No charge for deposits.

In addition, the Bank will cash all government checks of $400 and under at no charge, provided the payee is present and has proper identification. This service is provided for customers and non-customers.

The Bank has no history of closing branches in St. Louis and at this time has no plans to close any branches in low to moderate income areas.

The minimum deposit to open a savings account will be $50.00.

5. MARKETING AND PROMOTION

The Bank recognizes the importance of "word of mouth" marketing and intends to work closely with neighborhood organizations to explain the features of the Community Reinvestment Program. Advertising, promotional and explantory materials will be furnished by the Bank and distributed throughout the neighborhoods through the neighborhood organizations. The Bank will continue to advertise credit availability in media which are designed to reach the qualifying areas.

6. LIASON

Essential to the success of the Community Reinvestment Program is close liason with all interested neighborhood organizations. Interpretation of the Program to all who are interested in basic banking services is necessary and needs to be implemented not only by officers of the Bank, but also by members of each organization. By working closely together, the Bank and qualified organizations can not only help each other, but can help to revitalize a City and provide more and better housing for all its citizens.

7. Boatmen's Bancshares, if successful in

banks part of this Program.

8. MEETINGS

The Bank recognizes the importance of meeting with participating neighborhood associations to observe the success of the Program and to formulate better ways and means of delivering the Program to the neighborhoods. Officers of the Bank who are responsible for the Program shall be available for periodic meetings and for consultation at all times.

Sincerely,

Ethan A. H. Shepley, Jr.
Vice Chairman of the Board

EAHS,Jr./ms

FILE COPY

THE BOATMEN'S
NATIONAL BANK
OF ST. LOUIS

ONE BOATMEN'S PLAZA
800 Market Street, Box 236
St. Louis, MO 63166-0236
314 425-7500

JOHN L. WHITE
Senior Vice President
314 554-7976

February 23, 1989

Mr. John Hickey, ACORN Head Organizer
Missouri Association Of
Community Organization For Reform Now
1425 Tower Grove
St. Louis, MO 63110

Dear Mr. Hickey:

Thank you for your third and fourth quarterly Community Reinvestment Program Partnership report. As usual it's evident ACORN has done another excellent job in helping us with this important program.

I'm sure you will be pleased with the program results outlined in the enclosed reports. I have included a report for 1988, a summary of the three program years and the 1988 performance by census tracts and zip codes. You will note that we have now exceeded our original goal of $50 million by more than twice - nearly $103 million.

In addition to these loans, Boatmen's is participating in three MHDC low/moderate income home and home improvement programs. They are the first time home buyer programs in St. Louis City and the four Missouri Counties in our market area. The County loans are moving well but we could use your help with the City program. We have nearly $2.5 million in loans available for St. Louis City first time home buyers. The interest rate is 8.45% for 30 year fixed rate loans. FHA/VA underwriting standards are required but I think there should be a significant number of families that could take advantage of this program. One drawback may be that 4.25 points are charged but I think I may be able to get the City to help with them. Let me know your thoughts on this, if you will.

I look forward to seeing you Wednesday evening, March 8 at 7:00 p.m. Call me if you have any questions.

Sincerely,

John

John L. White

JLW:rgm
cc: W.J. Tice

The Oldest Bank West of the Mississippi / A Subsidiary of Boatmen's Bancshares, Inc.

THE BOATMEN'S NATIONAL BANK OF ST. LOUIS

COMMUNITY REINVESTMENT PROGRAM

PROGRESS REPORT

FOR: 12/30/88

LOANS FOR REAL ESTATE/ (Low to Moderate Income Areas)	NUMBER OF LOANS	DOLLAR AMOUNT $000s
1-4 Family	212	$ 9,177
5 or More Family	7	$ 1,075
Home Improvement	524	$ 3,680
Residential Construction/Rehab.	59	$ 9,938
Other Real Estate	78	$ 17,133
TOTAL	880	$ 41,003

OTHER LOANS/ (low to Moderate Income Areas)	NUMBER OF LOANS	DOLLAR AMOUNT $000s
Student Loans	4069	$ 8,405
SBA Loans	5	$ 1,861
Other Installment Loans	2100	$ 18,814
TOTAL	6174	$ 29,080

COMMITMENTS/APPLICATIONS/REJECTIONS/WITHDRAWN	NUMBER
COMMITMENTS OUTSTANDING:	51
APPLICATIONS PENDING:	19
APPLICATIONS REJECTED:	16
APPLICATIONS WITHDRAWN:	6

Prepared by: John L. White
Senior Vice Preside

COMMUNITY REINVESTMENT PROGRAM
REAL ESTATE LOAN COMPARISON DATA FOR PROGRAM YEARS 1986-88

DATE PREPARED: January 31, 1989

This report provides information on the total number and dollar amount of various categories of real estate loans made under our Community Reinvestment Program during the years 1986, 1987, and 1988. Program Totals are provided for each real estate loan category and a Grand Total of all real estate loans made to date is provided at the bottom.

LOANS FOR REAL ESTATE (Low to Moderate Income Areas)	NUMBER OF LOANS		DOLLAR AMOUNT OF LOANS ($ 000s)	
1-4 FAMILY 1986	295		$ 13,630	
1-4 FAMILY 1987	205		$ 8,985	
1-4 FAMILY 1988	212		$ 9,177	
TOTAL		712		$ 31,792
5 OR MORE FAMILY 1986	34		$ 5,083	
5 OR MORE FAMILY 1987	25		$ 4,121	
5 OR MORE FAMILY 1988	7		$ 1,075	
TOTAL		66		$ 10,279
HOME IMPROVEMENT 1986	475		$ 2,097	
HOME IMPROVEMENT 1987	564		$ 2,897	
HOME IMPROVEMENT 1988	524		$ 3,680	
TOTAL		1563		$ 8,674
RESIDENTIAL CONSTRUCTION/REHAB. 1986	17		$ 1,182	
RESIDENTIAL CONSTRUCTION/REHAB. 1987	35		$ 6,776	
RESIDENTIAL CONSTRUCTION/REHAB. 1988	59		$ 9,938	
TOTAL		111		$ 17,896
OTHER REAL ESTATE 1986	26		$ 3,346	
OTHER REAL ESTATE 1987	50		$ 13,872	
OTHER REAL ESTATE 1988	78		$ 17,133	
TOTAL		154		$ 34,351
PROGRAM GRAND TOTALS:		2606		$ 102,992

Prepared By: John L. Whit
January 27, 1989

COMMUNITY REINVESTMENT PROGRAM
COMMERCIAL LOAN REPORT

DATE: (From) 1/1/88 (Thru) 12/30/88

	CONSTRUCTION/REHAB LOANS ($000's)						MORTGAGE LOANS ($000's)					
	RESIDENTIAL (02)		MULTI-FAMILY (03)		CONSTRUCTION (01)		1-4 FAMILY (05)		5 OR MORE FAMILY (06)		(04-07) COMMERCIAL LAND ACQUISIT	
IP CODE	#	$	#	$	#	$	#	$	#	$	#	$
3088												
3103											3	1504
3104	5	2287									1	153
3106												
3107	1	9					4	384			1	60
3108	1	300	1	90					1	195	3	600
3109	6	3803					1	163				
3110	3	529					2	87			3	3167
3111							1	25				
3112	2	50					1	110				
3113												
3115	2	81					1	30			2	347
3116	4	322					2	17	2	72	1	28
3118	1	94					2	141			2	107
3120							1	19			2	88
3121	1	35					1	17			1	139
3125	2	225										
3130	28	1981	1	89			10	638	1	143	5	673
3133	2	99										
3134					2	6760	3	93			1	20
140					2	180						
143	1	118					3	133	2	102	1	58
147							2	35			6	666
TALS	59	9938	2	179	4	6940	34	1892	6	512	32	7610

Prepared By: John L. W
January 27, 1989

COMMUNITY REINVESTMENT PROGRAM

MORTGAGE/HOME IMPROVEMENT LOAN REPORT

(Reported by Census Tracts/All Figures Expressed in $000s)

ST. LOUIS CITY

DATE: (From) 1/1/88 (Thru) 12/30/88

CENSUS TRACT	MORTGAGE LOANS 1-4 FAMILY		HOME IMPROVEMENT LOANS 1-4 FAMILY		MULTI-FAMILY (5 or More Units)		NON-OCCUP 1-4 FAMI (INCL. IN CO	
	#	$	#	$	#	$	#	$
1015	3	91	4	15			2	6
1018	1	35	1	5			1	3
1021	1	41	4	62				
1052	3	158	6	16			1	4
1053	2	114	4	31			1	50
1054	2	38					2	38
1055	2	109	11	101				
1061			9	35				
1062								
1063			8	51				
1064	2	40	12	61				
1065	2	111	15	89				
1066	1	140	7	60			1	140
1067	2	87	10	82				
1071	2	83	5	18			1	50
1072	2	63	8	70			1	26
1073	4	90	19	147			2	41
1074	4	51	9	90			1	16
1075	1	12	14	125			1	12
1076	1	25	4	16				
1077			10	51				
1084	2	48	3	6			1	20
1085	1	14	3	23				
1096			10	83				
1097	1	11	10	63			1	11
1101	1	68	15	66			1	68
1102			8	67				
1103	2	45	4	22				
1104	1	22	3	25				
1105	1	58	5	26			1	58
1111	1	75	5	45			1	75
1112	2	65	4	24				

COMMUNITY REINVESTMENT PROGRAM

MORTGAGE/HOME IMPROVEMENT LOAN REPORT
(Reported by Census Tracts/All Figures Expressed in $000s)

ST. LOUIS CITY

DATE: (From) 1/1/88 (Thru) 12/30/88

CENSUS TRACT	MORTGAGE LOANS 1-4 FAMILY		HOME IMPROVEMENT LOANS 1-4 FAMILY		MULTI-FAMILY (5 or More Units)		NON-OCCUPANT 1-4 FAMILY (INCL. IN COLUM	
	#	$	#	$	#	$	#	$
1113	1	19	5	17				
1114	2	56	3	11	1	107	2	56
1115			2	18				
1122	1	90	3	12			1	90
1123	2	96	7	45				
1131			2	23				
1134								
1152	1	15	5	30	1	320	1	15
1155	4	146	6	17			2	74
1156	6	336	7	34			4	219
1157	2	71	3	23				
1163	3	202	4	16	1	242	1	44
1164	6	180	3	12			2	56
1165	2	111	8	59			2	111
1171	2	55	2	11			1	18
1172	11	767	11	126			5	248
1173	3	153	6	37			1	38
1174	10	441	5	25			4	130
1181	1	67	1	8				
1184								
1185					1	65		
1186	1	82	1	13				
1191	2	297	13	151				
1192			2	6				
1193	2	103						
1201			2	44				
1202			6	30				
1203	1	34	5	85			1	34
1211								
1212			1	1				
1213			2	11				

COMMUNITY REINVESTMENT PROGRAM

MORTGAGE/HOME IMPROVEMENT LOAN REPORT

(Reported by Census Tracts/All Figures Expressed in $000s)

ST. LOUIS CITY

DATE: (From) 1/1/88 (Thru) 12/30/88

CENSUS TRACT	MORTGAGE LOANS 1-4 FAMILY		HOME IMPROVEMENT LOANS 1-4 FAMILY		MULTI-FAMILY (5 or More Units)		NON-OCCUPANT 1-4 FAMILY (INCL. IN COLUM	
	#	$	#	$	#	$	#	$
1214								
1221			1	10				
1222								
1224	1	50	2	13				
1231	3	108	8	77			1	24
1232	5	339	6	28			2	200
1233	5	555	7	38			4	455
1234	2	150	4	69			1	90
1241	2	71	3	17			1	36
1242	4	196	5	18	1	28	3	178
1243	10	355	10	109			3	57
1246	2	61	2	9			2	61
1257			1	45				
1266	2	44	5	25			1	34
1267	3	66	4	28	1	67		
CITY TOTALS	149	7010	403	2926	6	829	64	3022

COMMUNITY REINVESTMENT PROGRAM

MORTGAGE/HOME IMPROVEMENT LOAN REPORT
(Reported by Census Tract/All Figures Expressed in $000s)

ST. LOUIS COUNTY

DATE: (From) 1/1/88 (Thru) 12/30/88

CENSUS TRACT	MORTGAGE LOANS 1-4 FAMILY		HOME IMPROVEMENT LOANS		MULTI-FAMILY (5 or More Units)		NON-OCCUPANT 1-4 FAMILY (INCL. IN COLUMN	
	#	$	#	$	#	$	#	$
2121	21	548	26	195			14	343
2128			2	9				
2136	3	91	7	48			1	41
2138	3	95	13	73			1	32
2139			4	13				
2140			1	2				
2141			4	26				
2160			4	18				
2161	2	304	5	58	1	246		
2169			2	11				
2181			1	5				
2190	7	290	5	41			1	34
2203								
3104			1	12				
7007			3	12				
7013			6	34				
8009	1	22	4	19				
8011			3	18				
COUNTY TOTALS	37	1350	91	594	1	246	17	450
CITY TOTALS	149	7010	403	2926	6	829	64	3022
INCOME QUALIFIED	26	817	30	160			2	61
GRAND TOTALS	212	9177	524	3680	7	1075	83	3533

Senator DIXON. Thank you, Ms. Cunningham. Your testimony has been very useful and we will be asking you some questions.

I'm delighted to see the distinguished Senator from New York State here, Senator D'Amato, who's been an important member of this subcommittee. Do you have any statement, Senator D'Amato?

Senator D'AMATO. Mr. Chairman, unfortunately, I'm going to have to go back to the subcommittee which is holding hearings on housing, but I commend you for your leadership in this area and I'm certain that we will produce legislation that is going to address a number of the very legitimate concerns that community groups have expressed and that go to the essence of having the kind of participation by our banking system in the local communities that I think represents a fair balance representing the constituents and also understanding the necessity of the banks to make a profit, to make investments prudently.

So I look forward to working with you on this and I'd ask if I might be permitted to submit this statement as if read in its entirety.

Senator DIXON. That request is granted. We thank the Senator from New York State.

STATEMENT OF SENATOR D'AMATO

Senator D'AMATO. Mr. Chairman, I am always interested in insuring that the goals of the Community Reinvestment Act are being met. Of course, as with the bills on Government check cashing and basic banking, we must approach Senator Metzenbaum's bill on Community Reinvestment with a healthy skepticism.

Meaningful disclosure of CRA performance does not necessarily mean full disclosure. I have always supported the concept that a bank's overall performance in serving the community in which it is located is the public's business. This information must be available at a meaningful time and in a usable format.

This should be our goal in these hearings—to ascertain what changes might be needed to insure that quality information is available to the public on CRA performance. If the CRA is not being properly implemented we should then ask whether there is a need for legislation or whether greater oversight of the regulatory agencies would be more appropriate.

I note, Mr. Chairman, that you have assembled an impressive group of witnesses and I am certain that these hearings will be useful.

Thank you, Mr. Chairman.

Senator DIXON. We're delighted to have Charles Grice of the Community Reinvestment Institute of San Francisco here. In trying to figure out how a Californian got here, Mr. Grice, it suddenly occurred to me this staff is very, very devious in what it does. There are two here for the Senator from Missouri and two here for the Senator from Illinois. It suddenly occurred to me that the Senator from California is chairman of the Housing Subcommittee and that's probably how you got here. We welcome you, Mr. Grice.

Mr. GRICE. I'm part of your affirmative responsibility to reach out.

STATEMENT OF CHARLES H. GRICE, MANAGING DIRECTOR, COMMUNITY REINVESTMENT INSTITUTE, SAN FRANCISCO, CA

Mr. Grice. Mr. Chairman, members of the subcommittee, my name is Charles Grice. I'm the Managing Director of the Community Reinvestment Institute. We're new group formed last year, based in San Francisco. We're a nonprofit and dedicated to increasing the supply of lending to low income communities around the country.

I might also say it's a pleasure to be here on this distinguished panel and I commend the work of the committee today on the important issues you're pursuing.

CRI is committed to training banks, thrifts, local governments, nonprofit groups, and others involved in the CRA business as to how to take advantage of it. We came out of an orientation of believing CRA could be good for everybody—be profitable for the for-profit institutions, it can make a lot of sense for local governments, and it certainly made a lot of sense for low-income communities, including nonprofit community-based organizations.

We were founded last year as a neutral nonprofit entity and our principal mission is to do research on the longer-term issues of how to broaden and deepen CRA lending; the second part is how to educate people and teach them how to do it. There's an awful lot of uncertainty and confusion out there. I am here as the embodiment, I think, of a lot of those frustrations among lenders and borrowers on both sides of the CRA battleground.

During the first year we've done a number of things. We've held conferences and workshops around the country. We've trained hundreds of banks now on how to do CRA in very pragmatic ways. We've talked to a lot of nonprofit groups and worked with local governments on how to use CRA. I think that's the bigger medium-term interest in trying to get local governments involved in this.

First of all, let me say that I think it's important to point out there's an awful lot of confusion among lenders and borrowers. Nobody really knows how to comply with the act that the Congress created back in 1977. The regulatory standards are also very unclear. So while I think generally it's a good idea to work with the lending community and the borrowing community to tighten enforcement, changing the legislation at this time seems to me a bad idea.

Working with the regulators I think would be a better use of everybody's time. The *Continental Illinois* decision really made people sit up and take notice. That was the first time, as you know, out of 15,000 bank applications reviewed by the Fed, that anybody had been denied an application on CRA grounds. Everybody took notice. Our phone started to ring in a big way after that.

The joint policy statement likewise was also a very big gesture and people really take that very seriously.

I just came back from a conference in San Diego with 300 lenders and a number of nonprofit groups there. They're in a panic trying to understand how to comply with the joint policy statement of the Fed.

So the basic thrust of my testimony today is that I think we should let the joint policy statement work its business. It's only been around for 3 months. I see a lot of lenders scrambling to make loans to nonprofits or churches or local governments. I also see a lot of banks who are desperately trying to understand what exactly is meant by both the original Community Reinvestment Act and also by the policy statement.

Nobody really knows what CRA loans are and if you ask the regulators what a CRA loan is, it's a little like the definition of pornography. They know when they see it but they can't describe it very well. That is really doing a disservice I think to everybody on this panel and the entire lending community. They really want to comply. Bankers are generally very conservative people and if you give them a test they want to score well.

The problem now is that the standard is very unclear. It's hard to know how much is enough, for example. It's hard to know what a successful program is. You know if you're getting a good rating from the Fed that you're in good shape, but it's hard to know if you're in that nether-nether world someplace—and that's where most banks should be—somewhere around the average range.

Let me skip ahead to my recommendations. First, it's to go ahead and let the joint policy statement and new regulatory regime have some time. I'd give it a year and if we don't see more Continental decisions in the meantime and tougher regulations, I would say then it's time to change CRA in a fundamental sense.

Second, I think there's a big role for Congress in oversight. I would encourage you all to get out there and work with the regulators, the lenders and the borrowers and try to see what the frustrations are on their side. You folks have a very important role to play I would submit in teaching the regulators how to do their job and trying to encourage them to do their job. The hearings held last year went a long way toward encouraging the *Continental* decision and the joint policy statement. Both are important things.

I would encourage you to get out there and see how lenders now are required to assess the credit needs of a community. That's a very nebulous thing. We don't really know how to do that. I've spent a lot of time. We've got research people working on it. It's very unclear how you assess credit needs of a community.

Third, I would suggest that the shift in focus from the application process to the examination process is a good idea. I think the dialog that goes on in private between a regulator and the regulated lender is a sacred thing. It's a little bit like visiting a lawyer or a psychiatrist. These should be privileged discussions. In general I think disclosure of gradings is a good idea. I think disclosure of numerical gradings might be a bad one. I only say that with safety and soundness on the table with the House now considering the FSLIC bill. My sense is, if you had numerical ratings or a "worst" list in the CRA department, the media could get carried away and use that as a way to describe bank "X" and bank "Y" as doing a really lousy job and you can then see deposits run away. We've seen that in California with S&L's. You see deposits walking out of the parking lot. That's a dangerous thing.

Finally, I think that the public disclosure of grades is an interesting question. Perhaps it should happen. I would encourage you to look at local communities and what they're doing. The city of L.A., and the city of Boston have each hired consultants to do their own evaluations and prior to those evaluations being completed lenders in those cities are scrambling trying to make loans. They understand that once this publicly available data is released they could be embarrassed and they're trying very hard to comply. But again, we get back to this frustration. There's a lack of just basic understanding of what is a CRA program, what does a successful program look like.

Finally, I have to make a plea for more tools. We need secondary markets for low-income housing loans. We need standardized underwriting criteria. We need a way for banks to do what they do best, and I should include S&L's, too, which is to originate loans. Banks do a good job of originating loans and selling them off to the capital markets. Right now that's hard to do in the very low income business. SRO hotel loans, homeless shelter loans, and loans to churches can't be bundled very easily right now and sold up the stream to insurance companies and pension funds. I think that's important if we're ever going to solve the problem. Let banks do what they do best and let S&L's do what they do best—originate these things and pass them upstream. That's where you're going to get the big bang.

Second, I would encourage people to think of how to broaden CRA to apply to other folks. I see the red light on, so I'll finish up. I think one place to look, is ERISA. If ERISA could be altered to allow pension funds purchases to include these types of securities, like low-income housing bundles, you might ultimately increase the supply of low-income housing.

Thank you very much.

[The complete prepared statement of Charles H. Grice follows:]

Community Reinvestment Institute
A Not-For-Profit Organization

TESTIMONY OF THE
COMMUNITY REINVESTMENT INSTITUTE
BEFORE THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS OF THE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

By Charles H. Grice
Managing Director
Community Reinvestment Institute
San Francisco, California
June 7, 1989

FULL TEXT OF TESTIMONY

Mr. Chairman and members of the subcommittee, my name is Charles Grice and I appear today as the managing director of the Community Reinvestment Institute, a newly formed organization dedicated to improving compliance with the 1977 Community Reinvestment Act. We commend you and your colleagues for your commitment to helping low-income America and for the continued interest in perhaps the U.S. economy's most interesting intersection of private benefit, public interest, and politics.

Community Reinvestment Institute

The Community Reinvestment Institute is committed to training banks, thrifts, community-based developers, government entities and other non-profits to understand, comply with, and take advantage of the CRA. We often use this training as an opportunity to organise pools of capital for low-income and business lending and to create models of "safe CRA" that are shared with other groups in other markets. Finally, we are beginning an ambitious research agenda in hopes of eliminating some of the roadblocks to increased investment by lenders, the broader business community, and individuals to low-income areas.

The Community Reinvestment Institute is located in San Francisco and serves both borrowers, lenders and local governments across the country. We are neutral, non-profit, and are governed by a board of directors including both lenders and borrowers. The Institute was founded in 1988.

During the CRI's first year, we held a major conference at the San Francisco Federal Reserve Bank, offered small-group workshops for lenders and non-profits around the country, undertook basic research on CRA compliance, and worked with local lenders, non-profit developers, and local governments to use CRA more productively. What emerges from this first year is firm evidence that the CRA responsibility, if managed well, can be a tremendous opportunity for a lender, local government or non-profit organization.

As an economist trained in public policy, and as one who has worked for the Senate, the Federal Reserve Board, a bank trade association, and more recently for a number of non-profits, I feel compelled to address the larger issue before this committee, namely, "How can Congress begin to move capital back into capital-starved neighborhoods?"

Improving the Community Reinvestment Act

Our testimony centers on three areas: how to improve the effectiveness of the CRA, the proper role of the application and examination processes, and the costs and benefits of public disclosure.

First, a few words about the current CRA environment. Almost twelve years of the Community Reinvestment Act have yielded little progress for anyone. Banks feel the CRA has been misused, non-profit groups feel CRA compliance is a sham, and the regulators have played guessing games with the intent of Congress. The CRA remains, however, a wonderful opportunity for the industry to reverse the effects of disinvestment in urban and rural areas and to meet new, and profitable, components of our communities.

CRA Successes are There

For example, we have spent the last several weeks working with several San Francisco-area banks to make a $6 million loan to a very low-income housing mortgage pool. The lenders, most of whom had never before worked with non-profits, loan poolers, or customers from the city's poorest neighborhoods, are excited by the opportunity to make this loan at cost. These funds will go toward the acquisition and rehabilitation of single room occupancy (SRO) hotels in the city's Tenderloin neighborhood.

Through the Chamber of Commerce and in conjunction with a major bank, two insurance companies, and a host of professional volunteers, we are organizing a social investors pool of individuals who will dedicate the use of their savings to the acquisition of transitional housing for the homeless. The lead bank will make a $1 million loan, backed up by the insurers, and be protected from interest-rate risk with 2% deposits from the investors.

As another example, the City of Boston has hired a consultant to study redlining as alleged by preliminary studies. Using publicly available statistics, the City has motivated bankers to create several interesting loan programs serving first-time homebuyers. And all of this before the data is even back from the analyst!

Los Angeles, Omaha, Atlanta, Detroit and a host of other cities have their own success stories, some driven by CRA protests, others by fear of Continental-type decisions, and still others simply by lenders caring to develop their customer base.

Fear and Confusion Remain

Some of the frustration and fear mentioned earlier, however, serves no productive purpose. For example, we receive calls every few days from lenders who are being asked to make cash contributions, marginal loans, or other non-traditional measures under the pretext of CRA. Some banks believe that underwriting a beauty contest or a rodeo constitutes a CRA activity. Others believe or are led to believe that a bank's affirmative responsibility is to its own employees only. Still others keep no records thinking the Act only applies to large, urban banks. Until everyone understands their responsibilities, and until these are clearly spelled out with helpful examples, CRA compliance will disappoint us all.

How Congress Can Help

Much remains, however, if the Congress and the federal government are to meet their own objectives, and indeed their own affirmative responsibilities. To improve the implementation of the CRA, we must all work to eliminate the bottlenecks, excuses, and wrong-headed thinking that impede capital from flowing whence much of it comes.

Recommendation 1: Let the New Regulatory Regime Take Effect

Recent actions by the federal regulators suggest that a golden age of CRA is at hand. Among other developments, the Federal Reserve Board's denial in February of the Continental Illinois Corporation's bid to acquire a small Arizona bank on CRA grounds and the Joint Policy Statement of the regulatory agencies in March indicate a radical shift in agency expectations of lenders. With the Continental decision, the Board said that ambitious plans and generous commitments are not enough. There must be evidence of an institutional commitment to CRA and there must be loans on the books.

The Joint Policy Statement, released in draft form the same day as the Continental order, struck a similar chord of fear in the rest of the nation's lending community. Lenders are hearing again and again how important CRA is and, in another break with the past, are receiving harsh CRA assessments from their once docile regulators.

I have just returned from a community lending conference on the West Coast sponsored by the Federal Reserve Bank and the Federal Home Loan Bank of San Francisco. The conference had over three hundred lenders and non-profits in attendance. Anyone there would have to describe the atmosphere as tense.

This tension is welcome. CRA is on the top of lenders' minds, making headlines in many of your home states, and becoming an issue on which Jesse Jackson and Jack Kemp agree. Surely something important is happening. Lenders and borrowers are learning to dance together, albeit with some clumsiness.

As with any change, these developments have a silver lining. First, the Continental decision and the Joint Policy Statement have not gone unnoticed. Lenders are now looking for loans, non-profits and other low-income customers are learning how to establish an on-going dialogue with these institutions, and the regulatory staff is quickly developing the expertise to help both parties work together. Finally, the Policy Statement tells lenders much more about how CRA should be done, how the data should be collected, and how a bank should relate this to the public. What was once a frustrating burden is less frightening and now much, much clearer. The intent of the Community Reinvestment Act of 1977 and the CRA of 1989 are fast becoming one.

Recommendation 2: Oversight

Above all, we would like to encourage the Committee and the Congress to exercise the oversight power so important to these issues. We respectfully encourage members of the Committee to accompany CRA examiners on a field visit, to hold hearings in your districts, to attempt to measure credit needs in lower-income communities, and even to participate in a CRA protest meeting. Only by seeing first hand these steps in the CRA puzzle can one begin to understand how good-natured, well-intentioned but woefully under-equipped are the lenders, borrowers and regulators in their struggle with the CRA.

Recommendation 3: Help Provide More Tools

The CRI suggests three other needs: tools, research, and disclosure. More and better tools are needed by lenders and borrowers to facilitate increased CRA lending. Secondary markets, standardized underwriting criteria for CRA-type loans, and credit enhancement mechanisms (e.g. mortgage insurance) are essential to increased lending.

Research is needed to help shape these tools and to broaden the number of participants and coordination of increased reinvestment. In particular, CRI proposes that Congress increase the amount of basic research on CRA-related issues, such as the nature and extent of CRA lending since the Act's inception, the role of non-bank lenders to urban and rural economic development, and the nature of other structural bottlenecks that inhibit capital from flowing to low-income areas. Furthermore, Congress should encourage the regulators to provide clearer examples of CRA activity and to make greater efforts at training regulatory staff, lenders, and non-profit CRA "customers".

Just as with research, the disclosure of CRA performance will promote longer-term compliance with the intent of CRA. The disclosure should be clearly understood, not mistaken for safety and soundness ratings, and be based on CRA examinations that are private, privileged, and frank. For the public, CRA disclosures should be "user friendly" and more current than at present. Congress should encourage the regulators to release agency summary assessments of lender performance, at most, and to protect the examination process as an opportunity for honest, harsh analysis of a lender's performance.

Only by making CRA lending easy, by organizing research and methodology to eliminate safety concerns and other excuses, and through phased-in, easy-to-use disclosure of CRA performance can Congress promote the process of community reinvestment.

Congress and the agencies should help make CRA easy and safe. We suggest the following specific measures:

1. First, both the lenders and the borrowing community need more tools for achieving our goals of increased capital formation, job creation, and prosperity. Secondary markets for low- and very low-income housing and small business lending would be enormously helpful in eliminating the mismatch between needs of borrowers and missions of banks. thrifts, and insurance companies. Enabling the secondary marketing of CRA loans would make CRA lending consistent with modern capital markets.

Under the current framework, banks make short-term construction and bridge loans, savings and loans hold some longer-term notes to maturity, and the bulk are sold into secondary markets. For CRA-style loans, often involving patchworks of equity and income streams, there are simply no existing mechanisms for pooling these loans under a generic category for sale to long-term lenders. We need a method of standardizing underwriting criteria and creating credit enhancement mechanisms.

2. Second, the Congress should look to broadening the base of

lenders covered by the CRA. As you know, only federally-insured depository institutions now are covered, leaving the largest holders of capital -- pension funds, insurance companies, brokerage firms, and other financial intermediaries -- without the responsibility and opportunity to reinvest. We suggest Congress review ERISA and other restrictions that may impede pension fund investment in affordable housing.

3. Congress must examine the government's housing agenda with an eye to using existing resources and new resources more creatively. CRA protests are driven by the lack of a federal housing policy.

4. Congress and the regulators should work together to see that there are sufficient staff in the field to emphasize CRA examinations, particularly at the FDIC. Attention must be given to drawing on the existing expertise in the Federal Home Loan Bank system, an expertise that should not be sacrificed in the Agency's reorganization.

5. Research is needed to help shape these tools and to broaden the number of participants and coordination of increased reinvestment. In particular, CRI proposes that Congress increase the amount of basic research on CRA-related issues, such as the nature and extent of CRA lending since the Act's inception, the role of non-bank lenders to urban and rural economic development, and the structural bottlenecks that inhibit capital from flowing to low-income areas.

6. Congress should consider the need for training. There is a great need among non-profit developers and small business groups to better understand how loan decisions are made, what comprises a good business plan, and how to take advantage of complex low-income tax credits, rehabilitation loans, and the myriad of local, state and federal programs. Only by helping shape CRA customers and by establishing a common analytical framework can the Congress and the agencies hope to achieve their objectives.

Recommendation 4: The Focus Belongs on the Examination Process

In your invitation to appear before the Committee, you asked today's participants to suggest the proper emphasis for CRA: the examination process or the application process. Obviously, both are critical to complete enforcement of lenders' responsibilities and borrowers' rights.

As you know, the Joint Policy Statement shifts the compliance burdens of borrowers toward the examination process. The draft statement was more energetic in this shift, requiring community organizations to maintain a running commentary on virtually every institution in order to protect their right to protest an application.

Happily, the Joint Policy Statement retreated to simply noting when comments were filed and, presumably, granting greater weight to comments filed before an application was submitted by a lender. This seems a far more reasonable procedure, especially in the kind of active takeover market that is emerging among banks and thrifts.

The CRI believes that every effort should be made to enforce the CRA primarily through the examination process, i.e. through the relationship between the lender and her examiner while protecting the community's right to intervene any time including the application period.

Again, Congress might play an important role in this issue by actively conducting its own review of lender performance. Just as Los Angeles, Boston and Atlanta are doing government-driven examinations of lender performance under the CRA, the CRI encourages this Committee to consider undertaking its own hunt for good and bad CRA performance. We believe the exercise to be beneficial for the Committee, the lending community, community-based organizations and the regulators.

In order to measure where we are and where we might go, the CRI recommends that the new policy guidelines of the regulators be given at least a year of testing in the marketplace. Lacking other major denials and/or significant changes in the volume of CRA lending, our recommendation would change.

Recommendation 5: Increase Public Disclosures

Recently there has been a great interest in public disclosure of numerical ratings, qualitative assessments by the regulators, or other indicators of lender performance under the Act. While we believe disclosure to part of the long-term solution, we would encourage prudence. Financial markets and their consumers react wildly to information that might reflect on safety and soundness of an institution; a poorly-interpreted CRA rating could cause dramatic, dangerous shifts in deposits.

This prudence should be tempered by several factors. First, whether or not Congress and the regulators act, city governments and others are performing their own public ratings of local lenders. In California, the City of Los Angeles is undertaking a year-long, carefully thought out assessment of lender performance that has the banks and thrifts in a panic. Several local non-profit groups are recording deed of trust transfers at City Hall, geocoding the loans, and tracking lender performance on a day-to-day basis.

Ironically, citizen groups in Los Angeles now know the

geographical distribution of CRA loans by lender by census tract months before the banks and their regulators. Almost two years before the annual Home Mortgage Disclosure Act statistics are released by the regulatory agencies, the community organizations are poised for their own very public, very embarrassing disclosure of lender performance.

Congress should consider making the reporting requirements more consistent and, therefore, more effective. In the last Congress, for example, the Home Mortgage Disclosure Act (HMDA) was amended to increase the reporting requirements of mortgage companies. This was an excellent step toward improving the statistics' usefulness.

Unfortunately, wholly-owned subsidiaries of holding companies still do not report activity outside the MSA of the parent firm. A simple extension of this responsibility would greatly enhance the value of the data.

It is important to remember that bankers are, by their nature, rather conservative folks. They enjoy performing well on exams and will work hard to meet the industry average. On the other hand, please recognize the value in maintaining the current carrot and stick approach. Ambiguity works for community organizations, especially in this environment. Setting clear standards, through explicit ratios or through equally deterministic public grades (relative or absolute), creates the opportunity for "gaming" and minimalism. The best standard is one established by the regulator with the strengths, capabilities and mission of the individual organization in mind.

The CRI recommends, therefore, the adoption of the Federal Reserve proposal in conjunction with the disclosure of more helpful public information.

Mr. Chairman and members of the Committee, thank you again for this opportunity to express our views. We welcome your questions and wish you well in your work.

Senator DIXON. Your testimony is very useful, Mr. Grice, because I kind of see it as a middle ground observation of this. Maybe I'll hear later my assessment isn't right, but that's the impression the chair gets.

If I may ask you, what is the Community Reinvestment Institute? What are you?

COMMUNITY REINVESTMENT INSTITUTE

Mr. GRICE. We have a board of directors of nine individuals, half lenders, half other people, including nonprofit folks, government people. I've got an advisory committee. My job as the managing director and I've got two additional staff is to run around the country and teach banks how to comply, talk to low-income community organizations and local governments—all three of those entities, and help them understand what their rights and responsibilities are.

So we're teaching everybody how they can take advantage of the act as stated, and also how to take advantage of the joint policy statement.

Senator DIXON. You're a business house?

Mr. GRICE. No. We're a nonprofit.

Senator DIXON. You're a nonprofit organization?

Mr. GRICE. That's correct. We are supported by fees that we generate from these presentations to for-profit entities and also by foundation dollars on the other side.

Senator DIXON. I see.

Mr. GRICE. We are also doing consulting work for city governments at this time. I'm currently doing one of these public evaluations. Cities are really interested in this.

Senator DIXON. Essentially, you bring the community groups and the banking institutions or the thrifts together and suggest a way you can make compliance with CRA regulations and so forth. That's kind of the work you do. The payment you receive for that, though, is not part of a profit institution. You are a nonprofit institution.

Mr. GRICE. That's correct.

Senator DIXON. So that your function, I take it, is to actually make this system work around the country. Is that a fair statement?

Mr. GRICE. Yes, sir. That's a fair statement.

Also, the second step. Once we do training, as in San Francisco where we're based, we try then to bring the nonprofits and the banks together to actually do pooled lending. I mentioned in my testimony a couple of programs going on now, exciting ones, where banks are making CRA loans for the first time. They didn't know what it was before and now they've got relationships with the nonprofit world and exciting things are happening.

Senator DIXON. I would like for you to give us your recommendations about ways that we could help bundle all this and move it upstream. You talked about the pension plans and other things. I like the idea. It may very well be a thing that we can take into consideration in the package we put together if we can get a consensus on the subcommittee and the committee for a package. So that would be helpful.

Mr. GRICE. I'll do that.

Senator DIXON. One of the things that comes through to this senator so clearly from the different perspective of all the different points of view that I hear here is that—and I don't mean this offensively to the Fed or in a partisan sense at all because administrations come and go but the Fed is here forever. There's some kind of a sense of not—I don't want to say failure—but sort of a lack of confidence in exactly how this has been handled at the regulatory level so far. I don't mean that critically to anybody on the board. I understand that staff level is where most of this is done.

But there seems to be a sense that maybe we don't quite yet know what we're looking for and how to do it because it came through to me from Mr. Wysocki—for instance, Jim Fitch is a man I know and if there's anybody among the bankers who's out there hustling around trying to help the community I think it's Jim Fitch on the basis of what I know about him as a person.

When you say Continental, I know a little about that case. I think there was a sense, if it wasn't a bum rap, at least it was surprising to find that more than 90 percent are 1 or 2 and Continental was a failure. This comes through even to a guy who doesn't have any expertise. I see that.

So I'm wondering whether some of the things the subcommittee ought to be looking at is how to determine how to better suggest good regulatory and supervisory performance in the Fed. One of the things beyond that, which I liked and which came from your remarks and maybe is implied in everybody else's, is perhaps more of a supervisory type of oversight hearing system in the subcommittee at least where we look at this on an ongoing basis and see how are you doing this year, ask whether it is improving some and what should be done within the system.

I tell you as a man who spent a long time in legislative affairs, only 9 years in the Senate but 20 years in the State legislature before that, you can pass all kinds of bills—my good friend was a Governor and knows that and he was in other executive positions as auditor of his State and other things—but my sense is that it's how they do it in the system that make laws work well or not work well at all, and I get an impression that maybe that's one of the things that's causing our problems here. We've almost got this down to where you're talking about whether you numerically rate them or not and I don't see that. I don't want to be offensive because I know the consumer groups see that as important, but I don't see that so much as the key to the problem.

I suspect other things are more of a problem than putting a number on them because it really comes through to me that you're putting a number on them now but you're not doing it very well if over 90 percent are getting 1's and 2's. I'd like to hear from you about that, Mr. Wysocki. You were moved by that statement.

Mr. WYSOCKI. All we have to deal with is the 90 to 95 percent that passes. We're not getting ratings on a case-by-case basis. That's why I was suggesting that, while reserving the right to challenge an application, we shift the discussion to the examination process, by saying what the rating is on a particular institution as a proposed rating. Let the debate and let the challenge be about the rating and we would get a more effective examination process.

I do agree with Charles Grice. There needs to be a clearer standard on CRA performance.

Now in the CRA statement, that both myself and Charles referred to, made in March by the regulators, they did have a couple pages in there that I think was a beginning of clarification.

One of my points would be that over the last 5 years with all of these different programs now, the programs we heard about in St. Louis as well as the ones Charles may be working on, the regulators should be able to set model programs for various sizes of institutions, even maybe regional ones, so that there's a differentiation between South Dakota and what California needs.

Senator DIXON. Well, let me interrupt you to say this. I don't have your expertise, but the panel should know I was State treasurer of my State for 6 years. In those days I had a program where you put money in institutions—as you well know, Mr. Wysocki—in exchange for a variety of things that they did in the communities—business development loans, student loans, in the rural areas agricultural loans, below the market rate when you had bad times and a lot of different things. And we would send to the institutions these indications of what you could do.

Well, don't they do that at the Fed?

Mr. WYSOCKI. Apparently not very well.

Senator DIXON. Well, I wonder why they don't at least do that and say, "Look, here's a whole list of a dozen things or twenty things you could do in the neighborhoods that we consider things that would be in your favor in a CRA evaluation."

Mr. WYSOCKI. Before Robin comments on that as being one of the lenders, let me just say my point here is let the market dictate the target goals, the target programs. Whichever institution has the best program in their particular size range, in their particular region of the country, let that set the expectations necessary to get a top rating against which other institutions are judged. First Chicago is different than Southshore Bank or South Chicago Bank.

Senator DIXON. Or a downstate bank.

Mr. WYSOCKI. Right. Let the market dictate.

Senator DIXON. They are different circumstance.

Ms. FOOTE. I would agree that the standards against which you're judged are very unclear. In fact, we have a CRA exam starting the middle of this month with 14 examiners coming out to examine us against this new policy statement, and while we believe that statement is a big step forward in giving greater clarification to what the examiners are looking for, it's really not all that specific. So it will be a learning process both for ourselves and for the regulators.

CREATIVE USE OF STATE FUNDS

I also wanted to address the idea that you raised about the creative use of state funds. I mentioned that we had increased our commitment with the Community Investment Corp. substantially. Of the $9.5 million increase, $4.5 was our revolving loan pool commitment, but $5 million represented a purchase of seasonal loans from CIC—kind of a private secondary market—which freed up money for CIC to reinvest in other projects.

What made that deal workable, since the rates on those loans were below market and therefore not investment grade, was that Jerry Cosentino committed to putting State funds into those banks which participated in taking the loans. So three of us—Continental Illinois, ourselves and St. Paul's Federal—are purchasing $15 million of loans from CIC and he's matching that with $18 million of 8 percent State money. That allows us to make a decent return on the investment.

Programs like this worked out through the various State and local agencies where they use their deposit dollars to benefit those corporations that are doing more are going to help make sure that this remains profitable.

Senator DIXON. Now enlighten me in this respect. Where in that process do you have some kind of a hearing where folks like Mr. Wysocki or Ms. Cunningham or Mr. Grice or anybody else can come in and say, "Well, with respect to this institution, we don't think they're doing it right or they ought to be doing this or they fail in this." Where is that happening?

Ms. FOOTE. Well, in our case, we have a review board for our neighborhood lending program.

Senator DIXON. Your bank does. But where is the community heard in that process where they rate your bank?

Ms. FOOTE. Right now today I don't think they are.

Mr. WYSOCKI. Only if the particular staff examiner knows who to call and takes the initiative to call.

Senator DIXON. Well, it occurs to me that that was one of the things that at least was implied in what you and Ms. Cunningham and others were saying, that there's not the true kind of full evaluation process that leads to the conclusion. Is the chair correct?

Mr. WYSOCKI. It's a case-by-case basis and that's a correct assumption. There's no way of knowing that. And if the staff turns over and goes on to something else in the agency, somebody else has got to start all over again.

Senator DIXON. OK. The Senator from Missouri.

Senator BOND. Thank you, Mr. Chairman.

A quick thought just crossed my mind. Mr. Clement, has "MOBUCKS" in Missouri been used in the community activities which you've engaged in?

Mr. CLEMENT. It certainly has. "MOBUCKS" is where our State treasurer makes available deposits at below market interest rates and we in turn are therefore able to lend those dollars out at below market rates to—it's specifically set up for small and minority businesses. Yes, we have used that and it is a viable program. I suspect in our State it was initially set up for the agricultural situation, but it has moved into the urban areas and many of the banks in the State are using that.

Senator BOND. Ms. Cunningham, I'm very impressed with the agreements that you worked out with the St. Louis banks, not just Landmark, but in your testimony you mentioned Boatmen's and Mark Twain and others.

Have you reached any similar agreements with savings and loans, in the St. Louis area?

Ms. CUNNINGHAM. At this time we have not. We just really haven't—well, some of them have just resisted us. Of course, there are so many financial institutions within the St. Louis area that we just take one at a time. We haven't gotten to them. I think we had about five different ones that we contacted and at this time we are only working with two of them.

Senator BOND. Are there other organizations like ACORN that might be working with the savings and loans?

Ms. CUNNINGHAM. Well, I think there's one other one, but they are not working with the same impact that ACORN is.

COMMUNITY PARTICIPATION

Senator BOND. I'd like to ask Mr. Wysocki a question. When you're talking about the community participation and the judgment of the rating, it seems to me that the real test would be not the rating that the examiner gives a bank, but the rating the community gives the bank.

Shouldn't you be in a better position to know who's working? You've already cited the outstanding examples and you ought to be conveying that and then I'm sure that there are some institutions that you've tried to work with—I assume, human nature being what it is—there are some institutions that you've tried to work with that have just rebuffed you.

Isn't that the most important thing?

Mr. WYSOCKI. It is, and that's one of the reasons I was suggesting that having public notice of when the exams were coming up would better enable the community to file comments.

To some degree, given the status of how the ratings are done, groups question how effective that is. But if there was public notice of an exam and you knew that the examiners were coming in, you could file timely comments and say,"Hey, I want to be talked to."

My other point would be I think the examiners need to do a better job of understanding their community and who should they be talking to. So I think there does need to be more three-way dialog at exam time between the regulators and the institution and the community. I think that would provide a more thorough exam.

Senator BOND. Ms. Foote, do you find the CRA to be expensive and costly, or is it one that you feel it is a profitable venture?

Ms. FOOTE. In terms of covering our direct expenses for the last 3 years we've made a small, very modest—in the $100,000 to $300,000 range—contribution to profit. We then have corporate overhead, rent, and other support costs that aren't charged directly. If you took all of those expenses into account, we would not make a profit.

Now part of the problem has been the variable nature of our rates, plus the fact that we peg starting rates to our home mortgage rates, including teaser discounts, which have been very deep. As a result, spread income is very low. We would expect that would be rectified over time, but I would point out that any department that is 100 percent invested in mortgage loans, which is basically what this is—this is why your comments on the secondary market are very much on point—is not going to stand much chance of earning an investor required rate of return.

You have only to look at the savings and loans. Take the top performing S&L's, the ones that are in no trouble but are performing well. Apply a 6 percent capital standard to them and look at their return on equity. There's not one that exceeds 12½ percent. Now that is not up to standard in capital markets for what you have to earn to be a viable, financial institution with a good, strong future.

Senator BOND. Well, let's not get into the savings and loan, but I think that some of the healthier savings and loans are the ones that stayed out of things other than home mortgages and we found that many of the better ones are the ones who stuck to their business.

Let me ask the same question of Mr. Clement. Does Landmark find this to be a cost?

Mr. CLEMENT. Well, I think if you look at the overall picture, in 1988, for instance, Landmark Bank devoted more resources, both human and capital to our CRA activities, and yet it was the most profitable year in the bank's history. In 1989, for the first quarter, we have devoted even more to this effort and the first quarter results I believe show that the shareholders are doing just fine.

Senator BOND. OK. Do you have any suggestions on how CRA should be changed from Washington, as opposed to what you might be able to do in St. Louis, legislatively or regulatorily?

Mr. CLEMENT. The way the law reads, or the way I interpret the law, and the way I see the statement that came out recently, it seems to me that maybe the framework is there. It's maybe that it is not regulated across the board the way it might be.

Senator BOND. Ms. Cunningham, I'd like to ask your views on how you'd like to see financial institutions meet their obligations? What would be the ideal performance for a financial institution in your community?

FINANCIAL INSTITUTIONS OBLIGATIONS

Ms. CUNNINGHAM. Well, Senator Bond, I'd like to say that over the years I have seen that financial institutions have not had much concern for the low income and moderate income within the community. And I would feel that their concern for that segment of the community would be what we'd need.

Senator BOND. Is that in making loans or contributing to community organizations.

Ms. CUNNINGHAM. Contributing to the community organizations is fine, but in making loans to people who have a low income—some of these are very responsible people, but their incomes are below the standards that are set by the banks. And then to pay a loan at today's prime rate sometimes is very difficult for these low-income people, but they are very responsible. And by lowering the interest rates as Landmark has done four points below their market rate has helped some of the citizens and also there are some other programs out there that have lowered the interest rates for home improvement loans, and this really has contributed to upgrading our community.

Senator BOND. Would you agree that that ought to be the focus of the CRA, getting the financial institution involved in making loans in the community and taking a direct role, like Landmark has done? Again, I think you cited some examples about Boatmen's in your testimony and Mark Twain and others that have taken a direct role.

Ms. Cunningham. Right. Getting them involved is important, but also knowing which banks are not complying with these needs is also important. I know personally some minority businessmen who can tell you that it's extremely difficult to get loans and many times they have to resort to sometimes closing their doors and other times they've been able to be skillful enough to get funding in some other way or to manage their businesses in some other way. But so many of the banks are extremely indifferent to their needs.

Senator Bond. You said that making loans to community organizations would be an acceptable way of avoiding a protest if they don't make loans but if they contribute to the community.

Ms. Cunningham. If they can contribute to the community by meeting the needs of the people who need these loans, that is the primary thing. That's primary.

Senator Bond. But some do just make grants instead?

Ms. Cunningham. Some do that, and I don't think that is acceptable. That is not an alternative.

Senator Bond. I would concur with that.

Thank you, Mr. Chairman.

Senator Dixon. I want to make three observations. We're going to go to the next panel now.

The first is that obviously we can't be as informed as you are in the time we give to you in these hearings. I hope every one of you here will help us by sending us in writing your suggestions about what we ought to do with this legislation, if anything. I guess the impression, for instance, Mr. Grice thinks we ought not to do anything on the legislation this year. But if he thinks that, then tell us what he thinks we ought to be doing in the agency itself in the CRA division of the Fed or other things that could improve this. We would appreciate your observations at whatever length you want to make it. Bear in mind that brevity helps some but keep to the point as much as you can, suggesting what we can.

I want to next observe that it comes through to this Senator and I think will be clear to everybody that follows this, that we need to do more inside the Fed with the CRA people in there to get a better result. I don't mean that critically of an individual because this is new and probably they don't know exactly what the result ought to be.

But I think we'll have one more hearing that has not yet been planned up until now on another day soon and get in a few of those people and ask them those questions. We will let all of you know what that day is and then you can give us the benefit about what you think about the exchange between the subcommittee and the people inside that agency that are supposed to be doing that work. I see that as helpful. We'll try that.

I want to say that the idea about the secondary market comes through very clearly to this Senator and my colleague and I intend to have a second hearing on secondary market issues. We probably can't get to that until September, but I see the relationship and we will do that.

Now also, let me say that we are going to send every one of you some separate questions in writing. Please give them the attention they deserve because that helps form the policy of what we ultimately do here.

But I leave this panel with the distinct impression that we are looking for some other things that aren't in this bill and that there are more things that can be done out there in the field to make this work better.

I would want to make a final observation here. I hear what Ms. Foote and others say and I see how there might be a limited profit in this, but I expect as you expand the base of the financial institution in the community and get that community's confidence for what you're doing out there, it isn't only the dollar you make so much as what it means for the long-term for the institution. You know, politicians grow over years by the services they perform. So do banks. So this is very, very useful. We thank you all.

The second panel is a consumer and banker's perspective: Jonathan Brown, the director of BankWatch; Allen J. Fishbein, general counsel, Center for Community Change; John M. Kolesar, president of the AmeriTrust Development Bank of Cleveland, representing the Consumer Bankers Association; and Charles G. Conville, president and CEO of PrimeBank Federal Savings Bank, Grand Rapids, MI, and treasurer of the National Council of Savings Institutions.

Gentlemen, you've been here a while and you observed that the chair himself tries to honor the red light. We would appreciate it very much if you would put your full statements in the record and then limit your remarks to the seven minutes allotted you and we thank you very much for being here.

Mr. Brown, we'll begin with you.

STATEMENT OF JONATHAN BROWN, DIRECTOR, BANKWATCH, WASHINGTON, DC

Mr. **Brown**. I appreciate the opportunity to testify this morning on hearings which I believe are very important to the neighborhood movement. I will focus my testimony on the issue of disclosure of the CRA evaluation and assessments at the agencies and Mr. Fishbein will examine more closely the issue of participation and application proceedings.

We believe that disclosure by the agencies of the CRA evaluations is essential to strong CRA implementation. In our view, CRA as a statute has inherent characteristics that suggest that it will be very difficult to have in the long run strong implementation without CRA disclosure by the agencies.

CRA is a very general statute. It does not have any precise regulations. There are no rules. So that if you look at the statute, if you're a banker or you're a member of Congress or you're a neighborhood group, it's very difficult to tell what is expected.

It's our feeling that it's only on a case-by-case basis can you really divine any sense for what the agencies' standards are, if they have any at all.

CRA in a sense is like case law I think in the judicial process. That is, you really have to look at the individual fact patterns over and over again to get a feeling for what the agencies expect.

Now because of that, it is clear that you need the best evidence of what those standards are, which is the CRA evaluation and the assessment, what the agencies, if they're doing their job correctly, carefully analyze the facts, reach their conclusions and then provide an explanation.

I think the disclosure of the CRA evaluations by the agencies not only will give us better insight into their underlying standards, but it will also tell us a lot about the quality of their examinations. If the agencies are doing a thorough and comprehensive job, it will be reflected in the CRA assessments they prepare. If they are giving CRA short shrift, then it will be readily apparent from the CRA evaluations.

I also think that CRA disclosure is vital to effective congressional oversight and review of CRA implementation. CRA addresses a set of fundamental issues which have been raised over and over again by the ongoing process of financial deregulation and I think you can capsulize these issues by asking the question: What is the proper role of a bank?

I think that there is an integral connection between CRA implementation in a broad sense and the very rationale for federal deposit insurance. I think it is the federal deposit insurance system which has allowed banks to make many nonstandardized loans, loans that cannot easily be sold in the secondary markets. Banks can hold these loans in their portfolios, these small loans, which no investor can be expected to evaluate.

In addition, banks have a broad retail network that has expertise in providing assistance in packaging credit. All of these functions in large measure exist and can be performed by banks because of Federal deposit insurance.

So I think that as Congress struggles with the difficult issue of Federal deposit insurance and its ramifications that it will need to think more seriously about CRA, what the proper standards should be, and what the proper role of banks should be in this regard. And I think that having access to the CRA evaluations of the agencies is critical for a proper decision making by Congress.

Now just briefly, in regards to what we think should be disclosed by the agencies when they disclose CRA examinations or CRA evaluations, it's our feeling that the assessments should be very detailed, that they should consider all the assessment factors, the facts reviewed, conclusions drawn, and in a sense that the CRA ratings, as apart from the written assessment, have been overblown in their importance.

The CRA rating itself is just a number. It doesn't tell you much about the underlying performance of a bank or the agencies' standards or, in fact, if it is not coupled with adequate information on the bank's performance, it could even be perverse because it would not increase confidence in what the agencies are doing.

In addition, I believe that if there is enough information on the bank's performance disclosed in CRA evaluations that the agencies make public, that many participants in the capital market, investors that invest in banks, can make their own independent judgment about the bank's performance. They can use the information provided in the evaluation and they can draw their own conclusions. They may be more interested in small business development than they are interested in low-income housing. But they will have some ability to make their own judgment.

Obviously, a prime example of this type of investor would be pension funds or State treasurers which are operating on placement of public deposits. You mentioned the link deposit program in Illinois. That's a very good example.

What has handicapped the implementation of these link deposit programs is that the decision making—generally speaking the State treasurer—has not had adequate information on banks' CRA performance. So they have been somewhat at a loss as to how to implement those programs.

Finally, I would suggest that what we really are talking about in terms of comprehensive disclosure would be essentially a disclosure of the agency's CRA examination report.

There could be some modifications. Certainly portions of the exam report which name individual organizations which provide information to the agency or comment on the personal behavior of individual loan officers need not be released. But with very minor modifications, the CRA examination reports could be disclosed. In fact, the House legislation last year really provided for that type of approach, the disclosure of the open section of the examination report, putting aside the closed section for dealing with privacy issues.

I think that the agencies themselves have a very strong kneejerk reaction to disclosure of "examination" reports of any kind and there's sort of a feeling of a domino effect, that today, the CRA reports; tomorrow safety and soundness reports.

We are mindful of that and certainly one could call it something else than the exam report, but I think it's clear that there's no reason not to disclose the information and it's really a question of how it's packaged to assuage the agencies' sensibilities.

I won't go into in any great length on the issue of the interaction between disclosure of CRA evaluations and participation in protest activities other than to say that the idea of penalizing groups for not participating up front at the time of the examination process or of imposing procedural limitations on the protesting process, I don't think that that is necessary. I believe that if proper CRA examinations are done and if they are made public, that that in and of itself will provide a very powerful incentive for neighborhood groups to participate up front in the process. If they don't, they will be handicapping themselves.

So I guess I'll close by referring to a good analogy which is a current movie which the theme is that if you build a baseball diamond in a Kansas cornfield people will come. I would say that if the agencies do good CRA exam reports and they make them available to the public, the neighborhood groups will come and there's no reason to intimidate them into early participation.

Thank you, Mr. Chairman.

Senator **Dixon**. Thank you, Mr. Brown. That's very useful.

Mr. **Fishbein**.

STATEMENT OF ALLEN J. FISHBEIN, GENERAL COUNSEL, CENTER FOR COMMUNITY CHANGE, WASHINGTON, DC

Mr. FISHBEIN. Thank you, Mr. Chairman and Senator Bond. It is a pleasure to appear before this subcommittee to testify on legislative reform of the Community Reinvestment Act and other low-income consumer banking issues.

The starting point for determining whether legislative reform is necessary is for this subcommittee to make a judgment about the adequacy of existing enforcement by the four regulatory agencies with responsibility under CRA.

A very compelling case for CRA reform made last year during the oversight hearings that Senator Proxmire held. The hearings showed that agency enforcement is lax and in need of a major overhaul. It is unlikely that the overhaul will occur without legislative direction.

Last year's testimony was rather devastating. This morning, you heard again that in any given year between 97 and 99 percent of all the institutions evaluated by the bank regulators receive excellent or good ratings.

It is this wholesale grading inflation that has completely undermined the effectiveness of CRA. The act's effectiveness will not change until we get more reasonable evaluations.

Now in an effort to see whether things have changed since last year—because several of the regulators last year indicated that they were in the process of upgrading their enforcement process—we asked the FDIC to provide us with a breakdown of the number of institutions that received satisfactory or better ratings, the ones receiving somewhat less than satisfactory ratings, and the ones with poor or unsatisfactory ratings.

We asked the FDIC because they are the one agency that will provide this type of information and I have set out before us what they provided. It is a complete printout of the institutions grouped by rating category. These are all the institutions receiving satisfactory or above. As you can see it goes on for about 75 pages. We estimate about 6,000 institutions. The second pile contains the list of institutions receiving somewhat less than satisfactory. It is two pages in length. I intended to include a third pile listing the institutions receiving unsatisfactory or poor evaluations, but as you can see there are no names. It is just a heading.

Senator DIXON. As an old trial lawyer, I'm always impressed by demonstrative evidence.

Mr. FISHBEIN. I thought you would be, Mr. Chairman.

The printout illustrates the continuing problem and until we get over that hurdle we are unlikely to see improvements in the CRA's effectiveness.

Last year, we proposed to the full committee a four-point legislative reform agenda. We still think those four points are necessary.

One is disclosure of the CRA evaluations, which Mr. Brown discussed.

The second key item is revising the rating system, at least on an interim basis, to make it comparative so that there would be a norm that institutions could be judged against and only those institutions that were doing better than the norm would be rated higher. Institutions that were doing a lot better than the norm would be rated with the top rating, number one.

A comparative rating system is needed because, as a number of witnesses this morning have testified, there are not adequate standards set out in the existing regulation and assessment criteria.

Now I would like to just address the specific issues I was asked to speak to in the invitation letter.

The CRA amendment to H.R. 176 that was discussed briefly by the full committee last year had several items, particularly the CRA disclosure, which in principle we can support. However, one which we find unacceptable is the notion that the procedural rights of citizens should be limited, in exchange for improving the examination performance.

We say that because it seems to be premised on a mistaken belief that the application process is too permissive, too cumbersome, or is being abused in some way. And that is just a fallacy. It has not been supported by the facts. We estimate that the number of applications which have been protested since CRA went into effect is about one-thousandth of a percent of all the applications processed. There have been about 300 CRA protests out of maybe 50,000 applications that have been processed by the regulators. It is a very rare event when an application is protested.

I noticed that Governor Seger mentioned in her testimony this morning that the difference in processing time between protested applications and nonprotested applications is only a few days.

The industry has never come forward with demonstrable evidence that indicates there is some kind of abuse of the protest process.

I raise these points because section 703 of the CRA amendment undercuts the procedural rights for citizens. It would establish a strong presumption in favor of the agencies internal review process regardless of the quality of the exam, and regardless of the strength of the evidence that is submitted by the protestants. In effect, it creates a higher burden of proof than already exists under current procedures.

And the provision also creates unneccessarily restrictive deadlines for processing applications. These deadlines run counter to the Administrative Procedure Act, which requires the agencies to develop a complete record when acting on any type of administrative proceeding.

It has been suggested that the purpose of this proposal is to shift the focus from the application stage to the examination, which is something we would hope to see happen.

But, as has been suggested by Mr. Brown, the way to do that is through improving the quality of the examinations and by disclosing CRA evaluations. Through this process, community groups, indeed all citizens, can be much more involved up front in connection with the examination process.

Until that happens, it is extremely important to keep the procedural rights of citizens in place regarding CRA protests. The protest process is a safety valve, to check abuses by the agencies. The protest is the one means that a group has if it is dissatisfied with an exam. If a group believes the examination process is not comprehensive enough they can turn to a regulator and present evidence that otherwise was not in the record. The protest is used as a last resort.

Compiling the information for a protest takes a lot of resources. It is a tremendous burden for community groups and that is why there have been relatively few protests over the years.

We urge the committee to consider improving the CRA examination process, consider disclosure, and the other reforms that I mentioned. However, we think it would be a mistake for the committee to see that as a tradeoff with limiting the procedural rights of citizens to participate in the application process under CRA.

Thank you, Mr. Chairman.

[The complete prepared statement of Messrs. Brown and Fishbein follows:]

TESTIMONY OF

ALLEN J. FISHBEIN
GENERAL COUNSEL

CENTER FOR COMMUNITY CHANGE

AND

JONATHAN BROWN
DIRECTOR

BANKWATCH

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

COMMITTEE ON BANKING, HOUSING & URBAN AFFAIRS

US SENATE

JUNE 7, 1989

Good morning, Mr. Chairman and members of the Subcommittee. My name is Allen J. Fishbein and I am General Counsel of the Center for Community Change and Director of the Center's Neighborhood Revitalization Project.* This testimony is presented on behalf of myself and Jonathan Brown, Director of Bankwatch. I welcome this opportunity to appear before this panel to present our views on legislative reform of the Community Reinvestment Act and on other banking matters of particular concern to the residents of modest income neighborhoods and communities.

Summary

Last year's oversight hearings on the Community Reinvestment Act (CRA) conducted by the Senate Banking Committee presented a clear picture that enforcement in this area has been seriously neglected for a long time by the federal banking regulatory agencies. More recent revelations about the Federal Home Loan Bank Board's mishandling of the savings and loan industry and new findings indicating apparent lending discrimination in a number of major cities has led to a "crisis in confidence" for many about the manner in which our financial institutions are supervised.

It should be obvious by now that the regulatory agencies are either incapable or unwilling to make substantial improvements in their enforcement programs. As we indicated in our testimony last year, a series of reforms are needed to strengthen CRA enforcement. A excellant starting point would be to require the regulators to disclose publicly the CRA performance evaluations for the institutions they supervise. We also believe that expanded disclosure about the lending practices of regulated financial institutions are necessary to curb discrimination against minorities.

Specifically, we support the CRA disclosure provisions contained in S.909 and the expanded loan disclosure requirements provided in S.908. Both of these bills have been introduced by Sen. Metzenbaum.

In addition, we urge your support for two additional bills. S.906, which would require banks to cash certain government checks for non-depositors and S. 906, which requires financial institutions to offer low income consumers access to basic banking services.

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* The Center for Community Change is a national, non-profit organization, based in Washington, D.C., that provides assistance to locally based low income community groups on a full range of community development issues. The Center's Neighborhood Revitalization Project is a leading resource for community groups on the Community Reinvestment Act, strategies for revitalizing low income neighborhoods, and techniques for assessing community credit needs.

Introduction

Earlier this year, US News and World Report ran a story on the Community Reinvestment Act. The article began as follows:

> Imagine an ideal government initiative: One that helps lower-income Americans own their own homes but does not breed welfare dependence, does not expand bureaucracies or budget deficits and does not hurt business or the economy. Such a program actually exists. It is called the Community Reinvestment Act (CRA). US News & World Report, A Housing Program That Really Works, Feburary 27, 1989, at 26.

US News astutely captured the paradox associated with CRA from its inception. The article goes on to acknowledge that the "law was ignored or undermined" by the regulatory agencies for years, but that despite its second-class status: "In places where it has been seriously applied and enforced, (CRA) has worked with surprising effectiveness." See attachment 1.

As I stated before the Senate Banking Committee last year, when CRA works it is usually in spite of the regulators and not because of them. CRA works because community groups have taken up where the regulators have failed. Under CRA, if a community is dissatisfied with the reinvestment record of a particular lender or if the residents of a certain area believe an institution's practices are discriminatory, they can challenge a pending expansion application by that institution. In many cases, these CRA challenges have resulted in settlements in which banks agree to upgrade their credit and deposit services to older urban neighborhoods and small growth communities.

What sometimes begins as a CRA challenge often results in the establishment of a new community reinvestment partnership between the financial institution, community groups, and local government. These community/lender partnerships are generating urgently needed resources into credit starved neighborhoods. The final report of the National Housing Task Force, chaired by James Rouse and David Maxwell, estimated that at least $4 billion in new loans commitments were attributable to CRA agreements.

CRA Agreements Can Make A Difference

Mr. Chairman, earlier today you heard from several bankers and community leaders about how CRA works. The witnesses who testified illustrate how former antagonists can learn to work together to revitalize their local communities. At the same

time, CRA has helped many lenders to discover new and profitable markets.

In scores of communities throughout the nation, CRA partnerships are beginning to produce results. Here are just two examples:

o In Philadelphia, Fidelity Bank and the Eastern North Philadelphia Initiative Coalition (ENPIC) entered into a three year reinvestment partnership as settlement to a CRA dispute. The agreement called for the institution to target home purchase loans to low income families using flexible underwriting criteria, provide financing for non-profit development corporations for the purchase and rehab of dwellings for eventual resale to neighborhood residents, and increased lending to locally based small businesses. After two years, the bank has made over 900 loans totalling more than $16 million under the terms of the agreement, an increase of nearly ten-fold for the bank's pre-agreement lending to the community.

o In California, Wells Fargo Bank reached a CRA agreement in 1986 with a statewide coalition of community groups and non-profit housing developers. The Bank set a first year lending goal of $41 million for low income housing, small business lending, and other targeted lending to low income consumers. To its surprise, Wells found that it far exceeded its lending goals in every category, making nearly $71 million in loans in the first year of the program alone.

My organization is just completing a survey of 15 major CRA agreements in fourteen major cities. As part of the survey we interviewed community leaders and bankers to discuss their attitudes about the success of the affirmative lending agreements. All of the community representatives we interviewed felt that the agreement had made a difference in the lending performance and attitude of the banks. Ninety-three percent of the groups pointed to additional new lending programs that have emerged outside the scope of the agreement, generating additional public and private sector resources.

Additionally, our survey found that more than two-thirds of the bankers responded that the performance of loans made under the terms of the CRA agreement were as good or better than for the rest of the institution's lending portfolio (the other respondents indicating that it was too early to tell). What is more, all the banks surveyed felt that the agreement had improved their relationship with the targeted communities.

In view of these successes, the challenge for the Subcommittee should be to preserve what has worked and to require improvements for what has not. In other words, " do not throw the baby out with the bath water." Clearly, the CRA evaluation process needs to be strengthened, but it must not be in exchange for weakening the public's procedural rights to challenge pending applications, as some have suggested.

Last Year's CRA Oversight Hearings Demonstrate the Need for Reform

In March 1988, the Senate Banking Committee conducted its first oversight hearings on CRA enforcement. The Center for Community Change, along with a number of other national and local community and civil rights organizations presented detailed evidence about the degree to which CRA enforcement had been neglected by the four federal banking regulatory agencies.

The Committee's former Chairman, Senator Proxmire, author of the original CRA legislation, asked the regulators about testimony indicating that sharp cutbacks had occurred in examiner time devoted to CRA enforcement, rampant grade inflation that assured virtually every lender of receiving a positive CRA evaluation and rating, and the agencies failure to use the application denial as a means for encouraging improvements in CRA performance. Proxmire was blunt. Opening the second day of the hearings, he told the regulators: "Frankly, it's time to raise tough questions and get serious responses, I wonder if your examinations are for real." Community Reinvestment Act: Oversight Hearings before the Senate Banking Committee, 100th Cong., 2nd Sess. 199 (1988).

The regulators response to criticisms of their enforcement record varied. One regulator acknowledge that insufficient resources were allocated to CRA enforcement, as well as to the other consumer compliance laws. Oversight Hearings, at 263. The others lamely sought to defend their record or promised to try harder in the future.

Recent Developments Raise New Issues About the Adequacy of Agency Enforcement

Since the March 1988, new information has come to light which raises additional questions about the agencies capacity and commitment to enforcement of CRA and the nation's anti-discrimination laws. Here is a brief chronology:

o May, 1988 the Atlanta Journal-Constitution releases its Pulitzer Prize winning series, The Color of Money. The study reveals that Black neighborhoods in Atlanta, regardless of income level, are far less likely to receive mortgage credit from banks and S&Ls than are White neighborhoods. See attachment 2.

o June, 1988 the Detroit Free Press publishes its own study of lending practices and finds that banks and S&Ls make home loans in the city's White, middle-income neighborhoods at three times the rate of similar Black neighborhoods. The Free Press also found that Detroit developers usually turned to lenders outside of the city to obtain financing, a problem which that paper noted may retard the city's revitalization.

o Additional research by the Federal Reserve Bank Boston and other researchers in New York City, New Haven, and other major cities reach similar findings as the Atlanta and Detroit studies.

o January, 22 1989, the Atlanta Journal-Constitution strikes again using information obtained from the Federal Home Loan Bank Board, the newspaper finds that on the average Blacks mortgage loan applicants are rejected twice as frequently by S&Ls than are Whites in 100 of the nation's largest metropolitan areas. The rate for Hispanics is 1.6 times higher. The data covered 10 million loan applications filed over a five year period.

o May, 1989, the US Department of Justice takes unprecedented action and launches a full-scale investigation of lending discrimination in Atlanta.

Prodded on by these revelations and by the pending CRA reform legislation, the agencies appear to be making some modest efforts to address their enforcement problems. This past March, the four agencies released a Joint CRA Policy Statement, indicating that they will be paying more attention to CRA enforcement. Earlier in the same month, the Federal Reserve Board denied an expansion application by Continental Illinois Bank on apparent CRA grounds. The first CRA denial of a bank holding company application ever. While community groups generally welcome these recent actions, experience indicates that significant reform will only come through legislative action.

Last September, we presented joint testimony to the full Senate Banking Committee, along with the Association of Community Organizations for Reform Now (ACORN) and Bank Watch. We testified in support of a series of CRA reforms that had passed the House Banking Committee last July.

Our testimony stressed that four major CRA reforms were needed to improve enforcement: 1) Overhaul the existing five-tiered CRA rating system to reduce the rating inflation that presently exists; 2) Improve agency accountability by requiring the public disclosure of CRA performance evaluations; 3) establish separate community and consumer compliance division within each of the four agencies with responsibility for conducting CRA exams; 4) expanding CRA coverage to include expansion by bank holding companies into non-banking activities. This last item was contained in the Bank Powers bill which passed the full Senate last year.

We urge this Subcommittee to act on these proposals this year.

The Procedural Rights Of Citizens In The Application Review Process Must Be Preserved

I indicated earlier in my statement about the need to guard against throwing the baby out with the bath water. Let me discuss this in further depth.

Even though it can be well documented that the CRA challenge process has proven to be an effective feature of the act, some have suggested that the public's procedural rights should be limited as some sort of quid-pro-quo for obtaining overall improvements in CRA enforcement.

Apparently, the public's right to challenge a pending application is unpopular with some banking groups, precisely because it has been so effective. There are some in the banking industry who have labeled community group efforts to challenge pending expansion applications as "extortion" or "blackmail". They suggest that protests by community groups are merely dilatory and in some way an abuse of the system. However, these critics have not come forward with evidence to support these allegations.

For example, I have heard some banking lobby groups repeatedly charge that CRA protests result in undue delays in processing applications. Yet, in its review of the issue, the Federal Reserve Board concluded that, on the average, CRA protested applications took only two days longer to process than non-protested applications which were subject to Board action.

Moreover, in the few cases in which CRA protests have taken many months to process, it has usually resulted from the applicant's failure to provide the regulator with sufficient information to complete its review.

Just as community groups are asked to document their charges about agency laxness, we would expect industry groups to come forward with evidence in support of their proposals for limiting citizen participation in the application process. To my knowledge, the banking industry has consistently failed to do this.

Comments on Legislative Proposals Before the Subcommittee

Mr. Chairman, you have asked me to present our views on several legislative proposals on CRA that are being considered by the Subcommittee. Specifically, the two CRA proposals that I am aware of that are before this Subcommittee are S.909 and the CRA amendment to H.R. 179 which was considered by the full Committee late last year.

S.909, introduced by Senator Metzenbaum directs the regulatory agencies to prepare a written evaluation of the lender's CRA performance after completing each CRA exam. The evaluation may exclude confidential information, such as the names of individuals. The bill provides for public disclosure of the numeric rating given to the institution and the basis for the rating, and discuss the facts about the lender's performance under each of the twelve CRA assessment factors as specified in existing regulations. The agencies are also directed to emphasize the lender's record of serving the housing credit needs of low and moderate income people, as well as the credit needs of small businesses and small farms, all of which were stressed when the Senate originally enacted the act in 1977.

The CRA amendment to H.R. 176 contains four basic elements: 1) it requires the regulators to publish written CRA assessments based on the CRA exam; 2) codifies the twelve CRA assessment factors contained in current agency regulations; 3) establishes a new procedure for soliciting public comments on an institution's CRA performance at the time of examination; and 4) revises the existing expansion application procedures as they pertain to public comments under CRA.

We strongly support the provisions in both bills that would require public disclosure of the CRA performance evaluations. As we have testified in the past, public disclosure of this information would be an important means for improving the examination process.

First, disclosure of these evaluations is a important accountability mechanism for the agencies. The release of these reports should provide a powerful new incentive for the agencies to conduct tougher and more thorough exams. Their failure to do so would be obvious to community groups, lenders, and legislators alike.

Second, disclosure would lead to a better understanding by both banks and community groups alike as to what is expected under CRA. For bankers it will provide them with the benchmarks they say they need to meet their obligations. Also, by providing more information earlier in the process it should reduce the need for many protests. In this sense, disclosure can be the catalyst for bringing banks and community groups together to work out their differences and enter into CRA agreements.

Third, disclosure will enable consumers to make intelligent comparisons about the lending records of their local financial institutions. It will help to spotlight those institutions with strong records, while encouraging poorly performing lenders to strengthen their performance.

In a limited sense, disclosure of CRA evaluations has been in effect. The FDIC regulations require the agency to prepare written summaries of the CRA records for banks applying for expansion applications. Unfortunately, these summaries tend to not be very detailed.

Further, New York State has a CRA law that is patterned after the federal law and has been disclosing summary evaluations for state chartered institutions for the past several years. NY also discloses the numerical rating it assigns its lenders.

Moreover, last year the Federal Reserve Board endorsed the concept of disclosure of CRA performance evaluations in its testimony before the House and Senate Banking Committees. Unfortunately, disclosure of CRA performance evaluations was not included in the Joint CRA Policy Statement issued by the agencies this past March. Nor are the agencies likely to mandate this type of disclosure without explicit direction from Congress.

After carefully comparing the disclosure provisions contained in S.909 and the CRA amendment to H.R. 179, we prefer the language contained in S.909. S.909 is somewhat more detailed about the types of information the agencies would be required to disclose.

S.909 also requires the five tiered numerical rating to be disclosed for each institution, while H.R. 179 does not. We recognize that several of the agencies have voiced concerns about rating disclosure, but it is worth noting that New York State has been disclosing the rating it assigns to its institution with no discernable adverse effect.

The most objectionable feature of the CRA amendment to H.R. 176 (Section 703) is that it attempts to substantially limit public participation in the application process as a tradeoff for disclosure of the CRA performance evaluations and other improvements to the examination process. Mr. Chairman, I think you will find that linking reduction in protest rights with

examination reform is completely unacceptable from standpoint of community groups.

Section 703 would have seriously undercut the procedural rights of citizens to raise concerns about the CRA performance of lending institutions in application proceedings. The provision would have established a strong presumption in favor of an agency's internal CRA evaluation, regardless of its quality, and against evidence submitted by protestants. Also, the provision imposes a much higher burden of proof on public participants who seek to obtain a public hearing.

The Joint CRA Policy Statement adopted by the agencies addresses this same point and hopefully obviates the need for Section 703. The Statement discusses the role of CRA examinations by stating that an institution's CRA record, as reflected in its examination reports, will be given great weight in the application process, and will often be a controlling factor. However, when a commenter raises signficant, factual allegations, the examination -- especially if it is not recent or does not address the allegations-- is not conclusive evidence. When this happens, the Policy Statement says, applicants should provide sufficient information that responds to the substantive issues, to help the agency reach a decision. Joint Policy Statement, at 14.

In any event, it is essential for the members of the Subcommittee to understand that intervention in the application process represents a safety valve for community groups to use should they be dissatisfied with the quality of the examination reports. Improve CRA exams, increase public confidence in the validity of the assessment process, and the focus of CRA will inevitably shift away from the application proceedings. However, citizens should continue to be afforded their full procedural rights should they believe the exams to be incomplete or faulty.

Lastly, although I have concentrated my testimony on CRA, let me stress that we fully support the low income consumer provisions offered by Sen. Metzenbaum and contained in S. 906 (Government Check Cashing) and S. 907 (Basic Banking Services Access).

In addition, we strongly support S. 908 (Fair Lending Oversight). This bill is comparable to legislation offered in House of Representatives by Chairman Henry Gonzalez and Rep. Joseph Kennedy (H.R. 898).

This completes my formal written testimoney. I would be glad to answer any questions you might have for me.

Senator DIXON. Thank you, Mr. Fishbein.

Mr. KOLESAR.

STATEMENT OF JOHN M. KOLESAR, PRESIDENT, AMERI TRUST DEVELOPMENT BANK, CLEVELAND, OH; REPRESENTING THE CONSUMER BANKERS ASSOCIATION

Mr. KOLESAR. Thank you, Mr. Chairman and Senator Bond. My name is Jack Kolesar and I'm president of AmeriTrust Development Bank in Cleveland, OH, but I'm here today in my role as chairman of the Government Relations Council of the Consumer Bankers Association.

Both I and the association thank you for giving us the opportunity to participate in these hearings. We commend both you, Mr. Chairman, and the Senator from my home State, for calling attention this way to the plight of urban neighborhoods.

Before I go into my prepared remarks, though, I have to ask the subcommittee's indulgence for certain handicaps that I bring to these deliberations. I'm from a small community development bank in Cleveland, OH, so I'm not nearly as smart as some of the other people that you're going to be hearing from on the first panel and on this panel. Everybody knows the bankers aren't nearly as smart as lawyers. If we were, perhaps there wouldn't even be a CRA for us to be amending in the first place. And we certainly are not as bright as the savings and loan people. Lord knows, I'd be a much richer man perhaps than I am. And I'm not even as sharp as your average banker because I came to this business through a very complicated route. Before I came to work for the bank I was a lowly social worker and before that I was a preacher.

So I don't know much about things like community ascertainment or——

Senator DIXON. I don't know if you're improving or going downhill, Mr. Kolesar.

Senator BOND. If he goes to law school, then we really ought to watch him, Mr. Chairman. That's the last refuge. [Laughter.]

Mr. KOLESAR. What I do know is what the law says and what working people need from their banks. The law says that banks should invest money in low and moderate income areas. So it seems to me that any tinkering we're going to do with that law ought to encourage banks to do that and ought to punish banks that don't.

Now as you're well aware, Mr. Chairman, not just from today's comments but over the course of the last couple of years in a series of hearings on this issue, there is a clear impression at least within the banking industry amongst my colleagues that CRA has deteriorated somewhat over the past 10 or 11 years into a fairly biased and ambiguous set of procedures in which banks are vulnerable to prolonged challenges to applications, protests that are based often on anecdotal kinds of evidence, and responsibility for meeting all of the credit needs of large urban areas.

In testimony before the full committee last fall, we cited various concerns regarding inconsistencies in the examination process and certain abuses we cited of the protest mechanism. And we took a fair amount of pride, though, on our testimony last fall in moving beyond that kind of reactionary criticism to propose a series of positive reforms to improve enforcement and to encourage banks to embrace their public responsibilities in a more proactive manner.

Specifically, our recommendations back in the fall included uniformity among the agencies concerning examination of rating procedures, regulatory analysis of community credit needs on a local basis, which could assist us the banks in identifying specific service opportunities, maximum time limits on CRA involvement in the application process, regulatory study of the impact on CRA lending of secondary market and private mortgage insurance practices you heard about earlier today, and also disinvestment by nonbank financial service providers.

Public disclosure of the regulator's assessment of an institution's CRA record we support very strongly, and a set of positive incentives for superior CRA performance.

Since that testimony back in the fall, two events have occurred which at least partially address those recommendations that we made.

The first was a series of actions on the part of the regulatory agencies, beginning with Governor Johnson's testimony that same day that we testified and culminating in this recent joint policy statement on CRA from all of the Federal regulatory agencies.

That sort of action goes a long way toward resolving our concerns for consistency and uniformity amongst the various agencies.

The second event and the more recent one is Senator Metzenbaum's introduction of S. 909 which occasioned these hearings. Now while his proposal certainly addresses the concern that we share with the neighborhood organizations and consumer groups regarding enforcement, we have serious reservations which are detailed in our written testimony regarding the evaluation of all assessment factors and the disclosure of the numeric CRA rating.

If we were to propose an alternative to the conflicting recommendations that come before this subcommittee and are currently under consideration in the House, that alternative would largely reflect the initiative proposed by Senator Proxmire in the waning hours of the 100th Congress last year, with certain modifications on that and one important embellishment.

I point out that our support for that Proxmire initiative involves no small concession on the part of the industry because it truly broadens the scope of the regulation and the law versus what it is today in a number of ways.

First of all, by establishing new assessment guidelines and criteria. Second, by encouraging public involvement in CRA evaluations at the time of the examination. Thirdly, by publicizing at least a summary of the CRA evaluations. Fourthly, by establishing some procedural rules for CRA protests during the application process that we would all have to live with.

We would add, though, to Senator Proxmire's proposal a set of positive incentives for banks to go beyond regulatory expectations in meeting those community credit needs. Details of those incentives are provided both in today's written testimony and in the comments we submitted last fall.

Briefly, we propose three things. First, is exemption from risk-based capital requirements for a bank's CRA-related assets. Second would be an expedited resolution of CRA protests for banks with a satisfactory CRA rating. And third would be immunity from protest for banks which consistently maintain the highest, most outstanding level of CRA performance.

It's our determination, Mr. Chairman, that a legislative synthesis, if you will, of the regulators' policy, Senator Proxmire's initiative, and our recommended incentives on the positive side would constitute the ultimate expression of a public policy that's designed to reward investment and to punish discrimination.

Thank you.

[The complete prepared statement of John M. Kolesar follows:]

TESTIMONY OF THE
CONSUMER BANKERS ASSOCIATION
BEFORE THE SUBCOMMITTEE ON
CONSUMER AFFAIRS OF THE COMMITTEE
ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
CONCERNING THE
COMMUNITY REINVESTMENT ACT

Presented by John M. Kolesar
President, AmeriTrust Development Bank
Cleveland, Ohio
June 7, 1989

Good morning, Mr. Chairman and members of the Subcommittee. I am Jack Kolesar, President of the AmeriTrust Development Bank, a community development bank affiliated with AmeriTrust Company, N.A., in Cleveland, Ohio. I am appearing today on behalf of the Consumer Bankers Association (CBA).[1] Both personally and on behalf of CBA, I must express appreciation for the opportunity to testify on the Community Reinvestment Act of 1977 (CRA), 12 USC Section 2901-05.

As your letter of invitation noted, CBA members have experienced their fair share of success in community development lending as outlined in my testimony before the full Committee on May 18, 1988. We have also recently catalogued the shortcomings of existing law and of recent ill-conceived House efforts to effect changes in this area in testimony before the full Senate Banking Committee on September 8, 1988. We do not, therefore, intend to cover the same ground other than by reference to the substantive details contained in those earlier efforts and the need to Congressionally address financial modernization (i.e., new bank powers) in tandem with any expansion in bank community service obligations.

Rather, our remarks today are focused on the procedural inequities and bias in the present treatment of financial institutions under CRA. We will also review the failure of legislative and regulatory developments since our last appearance here to address those inequities. Finally, we will offer some suggestions concerning potential refinements to existing law which could help redress those inequities and thereby further the objectives of CRA.

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[1] The Consumer Bankers Association was founded in 1919 to provide a progressive voice for the retail banking industry. CBA represents more than 800 federally insured banks and thrift institutions that hold more than 80 percent of all consumer deposits and more than 70 percent of all consumer credit held by federally insured depository institutions.

I. The Procedural Inequities and Bias Experienced by Financial Institutions under CRA

CRA instructs the federal regulators in very general terms to "encourage (financial) institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions."[2] This seemingly benign charge has been effectively rendered over time, an ongoing obligation focused solely on financial institutions and, rather specifically, on their record of satisfying the credit needs of low-to moderate-income neighborhoods. This process has de-emphasized the similar ongoing responsibilities of the federal regulators, the local communities themselves and other financial services providers to join with banks in addressing the credit needs of the entire community. Yet, these responsibilities are clearly contemplated by CRA's explicit recognition that banks can only "help" meet credit needs, and that there are, in fact, three other pivotal players in this drama - i.e., the federal regulators, local communities themselves and non-bank providers of community credit.

In our September 8 testimony, we inventoried the practical deficiencies in existing law and regulation. They include the absence of meaningful regulatory and public guidance in assessing and helping to meet community credit needs, inconsistent regulatory and public application of the CRA assessment standards, and outright abuse of the applications process. This creates a general procedural bias that places the burden of demonstrating satisfactory CRA performance wholly on the shoulders of the financial institution, especially in the face of an applications stage challenge. This bias prevails regardless of an institution's meritorious performance and regulatory assessment and in spite of the lack of merit, redundancy or even irrelevance of the challenge in question.

These are real, substantive criticisms. We submit them for the record not as a means to obstruct reform legislation but to paint in stark terms the degree of the problem from the view of the industry. Indicative of our desire to play a constructive role is a list, later in this testimony, of suggested improvements should legislation be contemplated. However, many in the industry frankly feel it is the financial institution which should protest the absence of meaningful regulatory and community assessments of local credit needs and wholly inconsistent CRA evaluations by different agencies or interest groups. They feel it is the bank that should be permitted to protest the regulatory proclivity to permit redundant and meritless challenges to run the same open-ended course as a legitimate protest. They feel it is the bank that should challenge the credentials and standing of community activists who recycle the same tired claims under the banner of ever-changing acronyms, often in a context wholly unrelated to their real interests or the CRA's substantive focus.[3] They feel it is the bank which should protest the almost total absence of meaningful regulatory or public CRA involvement and interaction outside the confines of the applications process where public advocates are most likely to come out of the woodwork, regardless of the merits of their claims, because this is where they have real financial leverage.[4]

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[2] CRA section 802(b), 12 USC Section 2901(b)

II. Recent Developments Do Not Redress The Existing Inequities

Since the Banking Committee last heard testimony on CRA, three notable developments have occurred. First, in the waning hours of the 100th Congress, Chairman Proxmire considered including in his financial reform package a CRA initiative (the Proxmire initiative) drafted by Committee staff in consultation with the staff of the Federal Reserve Board and both consumer and industry representatives. It was designed as a substitute for the CRA provisions in the House financial modernization bill, H.R. 5094, which were wholly unacceptable to the industry, the regulators and Senator Proxmire. The Proxmire initiative would have entailed a substantial expansion of existing law by (i) establishing new assessment guidelines and criteria, (ii) encouraging public involvement in CRA evaluations outside of the applications process, (iii) publicizing summary CRA evaluations, and (iv) establishing procedural rules for CRA protests during the applications process. While imperfect, the Proxmire initiative did attempt to encourage greater agency and community involvement and interaction outside of the restrictive confines of the applications process, and by establishing reasonable parameters around public involvement in that process.

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3. For example, Crestar Bank, headquartered in Virginia, has found its Virginia state bank acquisitions protested by the same Washington, D.C. principals, under different community organization names, who protested its Washington, D.C. national bank acquisition, based largely on the same grounds, i.e., the CRA performance of the national bank in Washington, D.C.; the involvement of the United Mine Workers in recent CRA protests of both Crestar and Manufacturers Hanover Trust Co. acquisitions has also piqued the industry in view of that union's bitter, protracted strike against a commercial loan customer of both banks and, in the words of a Manufacturers Hanover executive, "the absence of a mine-worker within 300 miles of the communities served" by the proposed acquisitions.

4. As an ACORN activist told reporters, "'When you're talking a billion-dollar merger, every day of delay costs lots of money. It's cheaper to negotiate than to fight.'" Gourevitch, Demands for Local Credit Shape More Bank Mergers, American Banker, June 2, 1986, at 17.

Second, in February 1989, the Federal Reserve Board issued revised CRA compliance guidelines and, in partial reliance on the new draft guidelines, rejected on CRA grounds an application filed by Continental Bank to acquire a financial institution in a Southwestern state.[5] Third, in March 1989, the federal regulatory agencies issued a revised version of the Federal Reserve guidelines in the form of a joint policy statement. To the agencies' credit, their joint statement also seeks to address some of the procedural inequities noted above by establishing a uniform interagency policy, providing some additional guidance concerning assessment requirements and criteria, and encouraging greater public involvement and interaction in CRA assessments and evaluations outside of the applications process.

But the policy statement, in fact, does little to truly correct the inequities faced by financial institutions under CRA. A uniform policy statement does not insure uniform application by the respective agencies. A policy statement recommending potentially useful "outreach" efforts an institution might adopt in assessing its community's needs is only partially helpful.

More helpful, however, might be a model of assessing needs. Institutions would like to see an exemplary assessment of a particular community on an experimental, "role model" basis. This is not to say that the model should be the standard measure in all cases. All communities and institutional capabilities are different. But we would encourage the regulatory authorities and community groups to undertake and share with financial institutions model assessments of their actual communities, given their expectations that this is precisely what every financial institution in the country is supposed to do.[6]

Further, while expressing a desire for greater public involvement in CRA evaluations and interaction with financial institutions outside of the confines of the applications process, the statement does little to foster that involvement. Indeed, it backs away from a positive step

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5. Interestingly, some consumer groups were as nonplused by this apparent "seachange" in Federal Reserve policy as was the senior management of Continental Bank, see L. Weiner, Community Groups Defend Continental, American Banker, February 21, 1989. Significantly, these groups had working relationships with Continental outside the confines of the protest mechanism. It should also be noted that the proposed target acquisition subsequently failed on May 19, 1989, see R. Ringer, Bank's Failure Spurs FDIC Anger Over Fed Ruling, American Banker, June 1, 1989, at 1.

6. In all fairness, we are advised that at least one such experimental assessment effort is underway at the San Francisco Federal Reserve Bank, focused on the community of San Jose (We are unaware of the progress and/or results of that project at this time). From remarks made by Charles Grice, President of the Community Reinvestment Institute (and others) at CRI's annual CRA conference at the San Francisco Federal Reserve Bank, San Francisco, CA, March 17, 1989.

in that direction which was included in the February Federal Reserve guidelines. In weighing a protest, the February guidelines would have permitted regulators to take into account the absence of a community group's involvement and interaction with the financial institution prior to the commencement of the applications process.[7]

Finally, the joint statement fails to address the procedural bias inherent in the applications process by refusing to foreclose extended, open-ended deliberations concerning an institution's CRA performance. By failing to place any specific temporal or evidentiary burdens on public involvement in that process, the statement facilitates abuse of the process such as that chronicled in our September 8 testimony.[8] Worse, this permits the regulators to disassociate themselves from the often confrontational and overreaching tactics attendant to many protests. They do so because the application record is considered to be incomplete in most instances until such time as every allegation, regardless of merit or redundancy, is at least responded to by the financial institution, if not actually investigated and resolved. We can assure you that there is no greater industry objection to the operation of the existing CRA scheme than this wholly biased applications procedure, where banks are subject to largely unrestrained criticism and delay, regardless of a satisfactory CRA record, or the lack of substance in a CRA challenge.

Senator Metzenbaum's bill, S. 909, does nothing to correct this procedural bias. Worse, it continues the public policy drift away from CRA's emphasis on the community as a whole and on the pragmatic limits on a financial institution's ability to serve that community's needs. It accomplishes these results by requiring publications of a written regulatory evaluation "of the institution's record of meeting the credit needs" of its community and by placing a "special emphasis" on low- to moderate-income housing, small business and small farm credit needs.[9] This initiative thereby ignores the CRA mission statement which is couched in terms of helping to meet the credit needs of the entire community, consistent with safe and sound banking practices.

S. 909 would in fact perpetuate and extend the procedural bias experienced by financial institutions under the current CRA. Proposed CRA section 807(b)(1) would require the publicized agency evaluation to state a conclusion "for each assessment factor" identified in the agency's implementing regulations, regardless of their relevance in a particular instance. In short, an urban center bank, with no rural farm credit relationships, could be faulted by the regulator and/or challenged by a community group due to the absence of such involvement, simply because small farm credit is on the regulator's laundry list of assessment factors. S. 909 seeks to turn that laundry list into a menu of required services, as opposed to the suggestive guideline it was designed to be. At best, any publicized agency evaluation should be required to address only those facts and factors deemed pertinent by the agency to the particular community's needs. These facts and factors will, of course, differ from community to community since no two communities will have the same needs.

Finally, CBA must voice a concern shared by the regulatory agencies relating to the bill's required publication of the agency's numerical CRA examination rating. The potential for public confusion of that rating with a statement of the institution's financial condition (i.e., a CAMEL or MACRO rating) is simply too great to warrant its consideration. In fact, the record deposit outflows in the savings industry, occasioned by the late breaking, sometimes incomplete, and often sensationalized media coverage of the FSLIC crisis, should give us all cause to generally reconsider any proposals calling for any disclosure of proprietary business and/or regulatory information at this time. This is particularly the case with respect to a rating disclosure requirement that would add nothing of substance to a well-crafted, narrative evaluation detailing an institution's CRA performance which is made publicly available. In this sense, the rating publication requirement is not merely unwise, it is wholly unnecessary.

III. Possible CRA Refinements

At the risk of some redundancy, CBA is compelled to restate some of its past recommendations concerning possible refinements to existing law. We will also address some additional ideas occasioned by the Subcommittee's letter of invitation.

Specific refinements which we have advocated in the past (and continue to support) include:

(i) mandatory interagency uniformity with respect to data gathering and reporting requirements (if any), as well as with respect to examination procedures and rating standards,

(ii) regulatory studies of community financial services needs which would assist the private sector in assessing and identifying specific community service opportunities, and

(iii) reasonable procedural limits on CRA-related public involvement during the applications process.

To these recommendations, we would respectfully submit that the following options continue to merit the Subcommittee's consideration:

(iv) Congressional hearings and/or regulatory studies of the extent to which secondary market underwriting practices (e.g., HUD,

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[7] This was also a positive feature of the Proxmire initiative considered as a substitute to the CRA provisions in H.R. 5094.

[8] The pertinent portions of our September 8, 1988, testimony are attached as Appendix A for ease of reference.

[9] S. 909, at proposed CRA sections 807(a)(1) and 807(b)(2), respectively.

Freddie Mac, Fannie Mae, S.B.A., etc.) may frustrate bank lending for low- and moderate-income housing, community development and small business purposes; such studies should focus also on the particular impact of private mortgage insurance underwriting practices on bank mortgage lending and might also address disinvestment by non-bank financial services providers, including insurance companies, securities firms, mutual funds, pension funds and similar corporate money managers,

(v) subject to satisfactory resolution of the concerns expressed earlier, some form of public disclosure of the regulators' general narrative evaluation of an institution's CRA performance, and

(iv) creation of some positive incentives for obtaining and retaining a desirable CRA performance rating, such as an exception from risk-based capitalization requirements for CRA-related assets and exemption from applications stage CRA challenge for some limited period after the receipt of a desirable performance rating.

A. Interagency Uniformity - Uniform interagency protocols concerning CRA performance data, conducting CRA examinations and rating CRA performances would provide much needed guidance to depository institutions as to performance expectations. It would also address concerns involving interagency consistency and the comparability of the CRA ratings rendered by different regulators. The Federal Financial Institutions Exam Council (FFIEC), comprised of representatives from the various federal regulatory agencies, would be a logical coordinating group.

B. Regulatory Study of Community Financial Services Needs - An oft cited criticism of existing law by both consumer groups and the banking industry is the absence of particular guidance as to the needs CRA is designed to address. Indeed, one prominent CRA authority has suggested that the law is "Kafkaesque" in the sense that bank's are forever defending themselves from charges of a crime which is never quite defined.

We do not propose that legislative or regulatory criteria should specify in detail the CRA obligation of financial institutions. This would defeat the purposeful flexibility in the existing law which acknowledges the varied needs of different communities. But we do believe that it is the appropriate role of government to aid the private sector in identifying community financial services opportunities which can be addressed to the benefit of all concerned.

Again, the FFIEC would be a logical coordinating body for such model assessment studies, which could be subcontracted to universities and other qualified research groups.

C. Maximum-Time Frames and Other Procedural Limitations on Public Involvement in the Applications Process - A major industry concern with respect to existing law is the open-ended nature of public participation in the regulatory applications process. Existing temporal guidelines generally provide that public participation must be permitted for specified minimum periods of time (i.e., the public comment period). Maximum time-frames are not mandated, however.

The absence of these latter limitations appreciably undermines the process of public involvement by discouraging concrete preparations and focused debate. This, in turn, tends to foster an unproductive level of frustration on the part of both industry and consumer participants, especially in the protest situation. Indeed, it is this feature that permits the community group abuses of CRA detailed more fully in the September 8 testimony. Maximum time frames are essential in our view.

Similarly, other procedural limitations should be considered, including regulatory discretion to weigh applications stage challenges in light of (i) their redundancy vis a vis previously resolved disputes, (ii) a desirable CRA performance rating, (iii) the currency or staleness of either the facts framed in the challenge or the CRA rating itself, and (iv) the previous involvement and interaction (or absence of same) by the challenging group. Such discretion would help alleviate the procedural bias borne wholly by banks in the applications process.

If the CRA exam and evaluation processes are satisfactorily reformed, the scope of CRA concerns that must be addressed through public involvement in the applications process should be narrowed appreciably. If the evaluations are perceived to be comparable and accurate and community service opportunities have been defined, there should be little to discuss when they are good and specific issues to address if they are bad. Indeed, if greater agency and public interaction and involvement outside the applications process are fostered, there should be far fewer legitimate protests. Maximum time frames and other reasonable procedural limitations should in no way infringe upon the public's interest in such a context.

D. Congressional Hearings and Regulatory Studies of the Impact of Non-Bank Underwriting and Disinvestment Issues - The significant role that secondary market and collateral insurance considerations play in a bank's lending and investment strategies cannot be overemphasized. As such, they directly impact a bank's ability to help meet community credit needs. Simply stated, assets and investments which are readily transferable and capable of prompt liquidation provide financial institutions the flexibility and protection necessary in today's highly competitive and often volatile marketplace. The growing interest in asset or receivables securitization in the banking industry exemplifies the strategic significance that the underwriting practices of non-banks may play in a bank's investment decisions.[10]

The advent of a "risk-based" system of bank capitalization will further heighten the significance of these factors. In fact, risk-based capital considerations are a primary area of concern to banks planning long-term community projects. Such undertakings may be rendered wholly unprofitable if they receive the high risk weighting which the capitalization formulas appear to require. For this reason, we recommend reduction or elimination of the risk-based capitalization standards in this area as more fully discussed below.

Another area over which banks have little control but for which the current CRA debates seem to hold them increasingly accountable, is community "disinvestment" by competing non-bank financial services providers, such as insurance companies, securities firms and other deposit-like service providers and money managers. This issue must be addressed if CRA is not to become a defacto substitute for responsibilities rightfully shared by all enterprises which benefit from the community's investments in their activities.

E. Some Form of Public Disclosure of the Agency Evaluation of CRA Performance - This is a highly controversial issue which tends to find significant disfavor within the regulatory agencies, unease within the industry and strong support by community groups.

The regulatory agencies are rightfully concerned that the disclosure of the numerical CRA-rating may be confused with a statement of the institution's financial condition (i.e., the CAMEL and MACRO rating), as discussed above. They are also concerned that public disclosure of any specific examination report information underlying a CRA-rating could subject their decisions to challenge under the Administrative Procedure Act, 5 U.S.C. section 101 et. seq., and in the courts.

CBA shares these concerns. However, we do believe that there may be merit in some form of public disclosure of summary conclusions concerning an institution's CRA-performance at the time a rating is rendered, provided that it is coupled with the applications stage procedural reforms discussed above.

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[10] Appendix B to our testimony chronicles the specific impact of a private mortgage insurance (PMI) company's policy of refusing to offer policies of less than $30,000. Notwithstanding credit-worthy borrowers and willing bank originators, the PMI company appears to have effectively "redlined" the Toledo community's low- to moderate-income housing market. Hearings on this subject would appear to be a useful supplement to the Subcommittee's housing related activities.

These reforms provide interested persons a more timely opportunity to express their concerns as to (and influence) an institution's record than is accorded by current law. They could help streamline a subsequent application process by focusing debate. Together, they would facilitate advance preparations and negotiations at the application stage and help alleviate the procedural bias experienced by financial institutions under existing practices.

F. Positive Incentives for Exemplary CRA Performance - The primary incentive for an exemplary CRA performance rating in the minds of far too many industry, agency and, yes, even community representatives is a negative one - i.e., avoid or limit CRA protests. As such, CRA itself has taken on a wholly negative image. Bankers label it as an excuse for extortion, the regulators cannot accept any mediating role, and community groups regard it as an opportunity to bash the banks.

If CRA is to effect its underlying goals, it must be freed from the procedural and attitudinal bias' we have reviewed today. Financial institutions must be encouraged to participate on a proactive basis, and those that already are must be rewarded accordingly. Those institutions in an aggressive application mode should be recognized for their proactive efforts and not penalized by the administrative, i.e., applications, process. This is the rationale for publicized evaluations and greater agency and community interaction and involvement - i.e., to spur greater efforts by all institutions, agencies and communities on an ongoing basis and outside of the applications process.

This is also the rationale for establishing the recommended procedural limitations on applications stage CRA evaluations. If the agencies and communities begin to do their fair share in helping banks to assess and address community needs outside of the applications process, that process can become the occasionally remedial (as opposed to routinely punitive) tool it was originally meant to be.

Most importantly, this is the rationale for establishing truly positive incentives for attaining a desirable CRA rating, such as a break on risk-based capitalization requirements and freedom from an application delay related to CRA concerns. The new capitalization requirements resurrect the specter of the old regulatory bias that, in part, underlies CRA's passage. Prior to CRA, CRA-type activities were prone to regulatory safety and soundness critiques when more profitable or less risky lending alternatives were available. Under the new capitalization rules, both senior management and shareholders may be similarly inclined if CRA assets are assigned a high risk rating. Why not avoid this very real likelihood by spurring CRA investment through a public policy-based reduction in or exemption from capital requirements in these areas?

Similarly, the thrust of CRA reform seems generally inclined in the direction of moving industry, agency and community engagement beyond the limited confines of the applications process and into a truly continuous and proactive partnership. Why not further encourage these results by specifically rewarding institutional success stories? Why not free banks from the prospects of meritless confrontations and costly delays for a year after they receive a desirable CRA rating?

CONCLUSION

The Consumer Bankers Association truly appreciates the continuing consideration of this Subcommittee and the full Senate Banking Committee on this and other consumer financial services issues. We hope we have helped the Subcommittee achieve some measure of understanding of the banking industry's concerns and frustrations relating to CRA. We have also attempted to summarize the most notable developments in this area, both in Congress and at the agencies, that have occurred since last summer. Hopefully, we have at least with some degree of objectivity highlighted the positive and negative aspects of those developments and offered some recommendations worthy of the Subcommittee's consideration.

In summary, we believe that to be effective, it is imperative that CRA be freed from the procedural and attitudinal constraints in which it is mired today. We respectfully submit that by removing industry, agency and public engagement in this area from the largely unproductive confines of the applications process so as to effect a true, ongoing CRA partnership, we can accomplish this result. We believe our specific recommendations are, as a package, a means to that end.

Senator DIXON. Thank you very much, Mr. Kolesar. I must confess I can't recall that by Senator Proxmire. Was that a bill?

Mr. KOLESAR. No, I don't believe it was ever actually introduced as a bill. It was in the waning days of the Congress and the debate was over the securities issue.

Senator DIXON. We'll develop that.

Mr. Conville.

STATEMENT OF CHARLES G. CONVILLE, PRESIDENT AND CEO, PRIMEBANK FEDERAL SAVINGS BANK, GRAND RAPIDS, MI; TREASURER, NATIONAL COUNCIL OF SAVINGS INSTITUTIONS

Mr. CONVILLE. Thank you, Mr. Chairman.

My name is Charles Conville. I'm president and chief executive officer of PrimeBank Federal Savings Bank located in Grand Rapids, MI. We are a $410 million, stock owned federally chartered savings institution. I am testifying today in my role as Treasurer of the National Council of Savings Institutions.

The National Council represents 500 savings banks and savings and loan associations in 37 States. These are both FSLIC and FDIC insured institutions. We represent approximately 35 percent of the industry's total assets.

Mr. Chairman, while the National Council does not oppose Senator Metzenbaum's bill, S. 909, we do not believe that any new legislation relative to the Community Reinvestment Act is necessary at this time.

Should Congress determine legislation is appropriate, the National Council could support the basic approach of this legislation. We would, however, strongly encourage that some changes be made to specific provisions of S. 909.

Section 13 of S. 909 requires that the public section of the written evaluation contain the institution's numerical rating, as required by the regulations implementing the Community Reinvestment Act of 1977 in effect on the date of enactment of this section. These numerical ratings, as I'm sure you're aware, and as Mr. Grice alluded to earlier, are the same 1 to 5 numerical ratings that are used by the regulators for the CAMEL or MACRO ratings for safety and soundness evaluations. In order to avoid even the remote possibility of creating confusion or concern in the mind of the public as to the safety and soundness of any insured institution, we would suggest that CRA ratings disclosed to the public be something other than numerical ratings.

For example, the public section of the written evaluation could use an alphabetical rating system as opposed to a numerical system.

The National Council feels that this is particularly important in view of the current financial status of the FSLIC, the number of insolvent institutions that cannot be resolved until legislation is finalized, and the great amount of publicity surrounding this situation.

Also, we would like to suggest two specific additions to section 1(c)(3) of S. 909. The first suggestion is that language be included to clarify that the appropriate Federal financial supervisor has discretionary authority to disclose to the institution information included in the confidential section of the written evaluation. This would be appropriate where the regulator determines that this would assist in the resolution of complaints or improve the institution's compliance.

Second, we would suggest that language be included in S. 909 stating that information included in the confidential section of the written evaluation not be considered part of the application process on the basis that the institution will not be able to respond to the complaint without access to specific information. An exception could be made where the information is available pursuant to our previous suggestion.

We've also been asked to address the question of shifting the focus of CRA from the application stage to the examination stage and whether the provisions included as amendment to H.R. 176 in the last Congress are the best means of achieving this change.

While the National Council does believe that this change in focus would be beneficial to both institutions subject to CRA requirements and to the communities in which they are located, we have reservations about specific provisions included in this amendment.

In view of the fact that current law provides for public notice of the availability of the CRA statement and files and solicitations and comments on an ongoing basis, we feel that an additional procedure in connection with the examination is both unnecessary to achieve the goals of the Community Reinvestment Act and burdensome to the regulatory authorities.

It does seem, in fact, more appropriate for the public to be encouraged to comment at any time as opposed to one time.

The amendment to H.R. 176 would have required a public notice of an institution's examination by the appropriate Federal supervisory agency prior to the examination and a notice that the public may submit comments on the CRA record of the institution at that time. In addition, the amendment would have provided for public comment on the report prepared by the regulatory authority.

The stated purpose of the Community Reinvestment Act is to require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions to encourage such financial institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions.

We believe that the goal of this legislation is better achieved at the examination stage rather than the application stage because of the regular scheduling of examinations which allows the goals of the 1977 legislation to be addressed on an ongoing basis.

Mr. Chairman, that concludes my remarks. Thank you.

[The complete prepared statement of Charles G. Conville follows:]

Statement of

Charles G. Conville
on behalf of the
National Council of Savings Institutions

before the

Subcommittee on Consumer & Regulatory Affairs
of the
Committee on Banking, Housing and Urban Affairs
of the
United States Senate

on
S. 906, S. 907 and S. 909

10:00 a.m.
June 7, 1989

Room 538, Dirksen Senate Office Building

Mr. Chairman, members of the Subcommittee, my name is Charles G. Conville. I am President and Chief Executive Officer of PrimeBank, Federal Savings Bank, in Grand Rapids, Michigan, a federally chartered, FSLIC-insured stock institution with over $410 million in assets. I am testifying today in my capacity as the Treasurer of the National Council of Savings Institutions. The National Council represents 500 savings banks and savings and loan associations in 37 states with assets in excess of $550 billion, representing approximately 35% of the industry's total assets.

The National Council appreciates having this opportunity to comment on the three issues currently being considered by the Subcommittee - changes in the Community Reinvestment Act of 1977, and proposals that would require the mandatory cashing of government checks and availability of basic checking services.

Community Reinvestment Act

The Community Reinvestment Act of 1977 (CRA), enacted as part of the Housing and Community Development Act of 1977, represents the most concerted effort of Congress to date to assure that consumers receive the credit opportunities to which they are entitled. Consistent with the language originally contained in the Banking Act of 1935, the CRA encourages banks and savings associations to meet the credit needs of local communities they serve, within the bounds of safe and sound practices. The National Council supports this public policy goal.

At this point in my remarks, Mr. Chairman, I would also like to emphasize that, in general, we view financial institutions' record of support for their communities as one of willing and good faith effort.

We do have some concerns with specific provisions of the bill addressing this issue introduced by Senator Metzenbaum, and we would like to offer our suggestions for changes that will address both the legitimate concerns of Congress and practical difficulties facing depository institutions.

The arguments advanced by the proponents of an expanded CRA are based on statistics that indicate that a large portion of financial institutions receive an acceptable Community Reinvestment Act rating (the "CRA rating") from their respective regulators. These individuals further argue that very few merger or other applications are denied as a result of unsatisfactory CRA ratings. The National Council believes that the regulatory authorities have sufficient authority under current law, and that recent reports of more stringent enforcement efforts indicate that improvements have been made in this area.

While the National Council of Savings Institutions does not oppose Senator Metzenbaum's bill, S. 909, we do not believe that any major new legislation relative to the Community Reinvestment Act is necessary at this time. Legislative proposals introduced in both the House of Representatives and the Senate during the past two years have clearly indicated the increased level of Congressional attention to CRA. This development, along with increased attention by the public, has served to increase general awareness of this issue.

As I am sure the members of the Subcommittee are aware, some states already have full interstate banking laws, and many other state laws will allow full interstate banking in the not too distant future. This activity will allow for further review of institutions' CRA performance as applications are filed for mergers and acquisitions.

S. 909 - To Amend the Community Reinvestment Act of 1977 to Require Written Evaluations

I would now like to address the specific provisions of S. 909, legislation introduced by Senator Metzenbaum to require a written evaluation by the appropriate regulator of an institution's record of meeting the credit needs of its community. Essentially, the effect of this legislation would be to provide to the public an evaluation based on the appropriate regulator's assessment conducted during the regular examination of the institution. The National Council of Savings Institutions supports the basic approach of this legislation.

We would, however, strongly encourage that some changes be made to specific provisions of S. 909. Section 1 (3) of S. 909 requires that the public section of the written evaluation contain the institution's numerical rating as required by the regulations implementing the Community Reinvestment Act of 1977 in effect on the date of enactment of this section. These numerical ratings, as I am sure the Subcommittee members are aware, are the same 1 - 5 numerical ratings used by the regulators for the CAMEL ratings to classify safety and soundness evaluations. In order to avoid even the remote possibility of creating confusion or concern in the mind of the public as to the safety and soundness of any insured institution, we would suggest that the CRA rating disclosed to the public be other than a numerical rating. For example, the public section of the written evaluation could use an alphabetical rating system as opposed to a numerical system.

The National Council feels that this is a particularly important point in view of the current financial status of FSLIC, the number of insolvent institutions that cannot be resolved until legislation is finalized, and the great amount of publicity surrounding this situation.

Also, we would like to suggest two specific additions to Section 1(c)(3) of S. 909. The first suggestion is that language be included to clarify that the appropriate Federal financial supervisory authority has discretionary authority to disclose to the institution information included in the confidential section of the written evaluation. This would be appropriate where the regulator determines this would assist in the resolution of complaints or improve the institution's compliance.

Secondly, we would suggest that language be included in S. 909 stating that information included in the confidential section of the written evaluation not be considered as part of the application process on the basis that the institution will not be able to respond to the complaint without access to the specific information. An exception could be made where the information is made available pursuant to our previous suggestion.

CRA Amendment to H.R. 176 (100th Congress)

We have also been asked to address the question of shifting the focus of CRA from the application stage to the examination stage, and whether the provisions included as an amendment to H.R. 176 in the last Congress are the best means of achieving this change. While the National Council does believe that this change in focus would be beneficial to both the institutions subject to CRA requirements and to the communities in which they are located, we have reservations about the specific provisions included in this amendment.

In view of the fact that current law provides for public notice of the availability of the CRA Statement and files and solicitation of comments on an on-going basis, we feel that an additional procedure in connection with the examination is both unnecessary to achieving the goals of the Community Reinvestment Act and burdensome to the regulatory authorities. It does seem, in fact, more appropriate for the public to be encouraged to comment at any time. The amendment to H.R. 176 would have required a public notice of an institution's examination by the appropriate Federal supervisory agency prior to that examination, and a notice that the public may submit comments on the CRA record of the institution at that time. In addition, the amendment would have provided for public comment on the report prepared by the regulatory authority.

The stated purpose of the Community Reinvestment Act is "to require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions." We believe that the goal of this legislation is better achieved at the examination stage rather than the application stage because of the regular scheduling of examinations, which allows the goals of the 1977 legislation to be addressed on an on-going basis.

S. 906 - The Government Check Cashing Act of 1989

As noted in the GAO Report to Congressional Committees of October 1988, entitled Government Check-Cashing Issues, "Nondepositor access to check cashing services is a difficult, complex, and emotional issue." According to this same report, "about 86 percent of banks and 55 percent of thrifts cashed U.S. Treasury checks for nondepositors. Of that total, nearly 56 percent of banks and 84 percent of thrifts cashed Treasury checks free of charge. For those that charged for the service, the median fee was about $2.00." This statement certainly indicates that many insured depository institutions are cashing checks for nondepositors at a reasonable fee. This same GAO report indicated that while there is evidence of some problems in this area, it could not locate any current reliable nationwide surveys that would enable policy makers to determine just how significant check cashing problems are for low- and moderate-income consumers.

Under these circumstances, the National Council of Savings Institutions would respectfully suggest that rather than enacting separate legislation, Congress consider including both government check cashing services and basic banking services as activities for which an institution be evaluated under the current Community Reinvestment Act. While the current statute addresses the credit needs of the community, it could be expanded to include the service needs of the community, including the service needs of low- and moderate-income members of that community. As an alternative, separate legislation parallel to the Community Reinvestment Act, addressing services rather than credit needs, could be enacted.

We feel that this approach has numerous advantages. First, there is some evidence included in the GAO's report to indicate that difficulty in cashing government checks varies by the size of the community and by individual community or state. The solution, therefore, should be tailored to the problem. Secondly, many depository institutions are already cashing checks for nondepositors at reasonable fees. Enactment of legislation mandating this service would impose some requirements such as registration and posted notices that seem to be both burdensome and unnecessary for institutions that are already providing this service.

In addition, enactment of a provision similar to Section 2 (4) could have the unintended effect of encouraging those institutions that do not currently charge fees for this service to impose them. Lastly, this approach would avoid any potential difficulties with inconsistencies between federal law and the laws that have been enacted in several states addressing this issue.

We would also like to suggest that the long-term goal of actions by the Federal government to address this problem should be to handle government check cashing by electronic funds transfer to the largest extent possible. This approach has the advantage of being less expensive for the governmental entity issuing the benefit, greatly reducing the potential for fraud for the depository institution, and providing much greater convenience for the recipient. The direct deposit method may also have the added benefit of increasing the personal safety of the recipient.

We would also like to take this opportunity to comment on several specific provisions of S. 906, the Government Check Cashing Act of 1989. First, we would suggest that the provision that was included in the government check cashing portion of H.R. 5094 that allowed the depository institution to impose a waiting period not to exceed 20 days after the registration is completed before cashing the first government check be included in S. 906 or other similar legislation addressing this issue. In addition, we would suggest that Section 422 (k)(1) of H.R. 5094 also be included. This provision would allow an institution to deny check cashing services in cases where there is reasonable cause to believe that either the check or the identification card has been altered or forged. Both of these provisions will help mitigate the exposure of depository institutions to possible fraud in connection with cashing government checks for nondepositors.

Lastly, the National Council would like to suggest that provisions requiring two reports by the Federal Reserve Board that were included in H.R. 5094 but not in S. 906 be added to any legislation enacted by Congress. The first report would address the questions of losses due to fraud and the "bottomline" cost to depository institutions to provide these check cashing services, and the second report is based on a feasibility study on

requiring the direct deposit of U.S. Government checks. We feel that these two studies will prove useful, particularly in achieving the long-term goal of using electronic funds transfer to the greatest extent possible.

S. 907 - The Basic Banking Services Access Act of 1989

We would like to comment very briefly on two specific provisions of S. 907 that are of concern to the members of the National Council. Under Section 2(d)(9)(B), a basic financial services account may be closed by the depository institution after notice to the individual by reason of the occurrence of "a pattern of fraudulent activity" involving the account of such individual. However, nowhere in the statutory language does the bill indicate what would constitute a "pattern of fraudulent activity." Nor does the proposed law consider the amount of losses institutions - especially smaller ones - might suffer before fraud could be proven. Such a requirement seems especially egregious when considering that the Uniform Commercial Code severely limits depository institutions' recourse against account holders.

Equally important, S. 907 fails to provide for a "means test" to determine whether an individual is entitled to open a basic financial services account. Although the proposed basic transaction services account is, in theory, available only to individuals with $1,000 or less on deposit at the institution, the statute as written fails to consider the individual's annual income or net worth. Lack of a means test could lead to abuse by those individuals who do not require a "basic" account yet want to avoid the fees associated with a normal account.

Relationship with State Law

The National Council of Savings Institutions has a concern of a general nature with both S. 906, the Government Check Cashing Act of 1989, and S. 907, the Basic Banking Services Access Act of 1989.

This concern is that, as is the case in many instances when the Federal government adopts a new law, inconsistencies develop with existing state law. It is our understanding that some states - including Connecticut and Massachusetts - have adopted their own laws to address the issues of government check cashing or basic banking services, or both. The immediate question that arises is whether federal or state law prevails in a situation such as this. We would respectfully request that any legislation adopted that addresses either or both of the issues grant the Federal Reserve Board the authority to determine when inconsistencies exist between Federal and state law.

Mr. Chairman, this concludes my prepared remarks. I would be happy to answer any questions that members of the Subcommittee may have.

Senator **Dixon**. Thank you. That's very helpful, Mr. Conville.

The Senator from Missouri.

Senator **Bond**. Thank you very much, Mr. Chairman.

Before I begin the questions, I wonder if we could have your permission to insert into the record some information my staff has about the CRA program of Boatmen's Bank in St. Louis. I think that would be helpful to this committee and its staff.

Senator **Dixon**. Since my checking account in Bellville is in a Bellville institution, I will permit you to do it.

Senator **Bond**. That should help with any overdrafts. I'm sure as a former treasurer you don't have that problem, but as a former auditor it still bedevils me.

[Committee insert of Senator Bond's information follows:]

In late 1985, the Boatmen's National Bank of St. Louis reorganized and formalized its Community Reinvestment Program (CRP). The program was designed to provide loans for the acquisition, rehabilitation, and/or improvement of housing-related real estate.

Boatmen's has had a long and proud history of working within the community to make St. Louis a better place to live. We took the best parts of a variety of programs to formalize this program.

Loan Programs and Guidelines

We committed to make $50 million available for housing-related loans in low- to moderate- income areas. The areas targeted were those census tracts in which median income was below 80 percent of the SMSA median income level in St. Louis. We also announced a neighborhood partnership program through which the bank made $100,000 available annually for grants to local neighborhood organizations. In return, these organizations agreed to help promote the CRP and assist the bank in loan packaging and client counseling. To improve the program's effectiveness, these neighborhood groups were also asked to provide input to the bank.

Today, these neighborhood groups are the a major factor in Boatmen's Community Reinvestment Program. They have generated loan referrals far in excess of what was anticipated. Of equal importance has been the counsel and suggestions they have offered to us as the program progressed. Their unique perspective is a crucial element of our program's success.

Although the CRP encompasses a variety of housing loans, our key focus is on providing financing for the purchase and rehabilitation of one- to four- family residences and low- to moderate- income, multi-family, residential buildings. To achieve this goal, a flexible approach is used in underwriting loans. While program guidelines must comply with safe and sound banking principles, emphasis is placed on finding ways to qualify applicants, as opposed to looking first at factors that might disqualify them. Although interest rates are at market, terms can be adjusted, for example, by extending the basis of amortization to as much as 30 years if that will help qualify the applicant. Loan-to-value ratios can be as high as 95 percent, and the debt-to-income ratio applied is the most liberal of any used to qualify applicants for any federally insured/guaranteed program. This ratio can be exceeded on a case-by-case basis where applicants have demonstrated an ability to meet a higher ratio. Historically, many people with low and moderate incomes have paid a higher portion of their incomes for housing than have more affluent people.

Past credit problems are also dealt with in a manner less stringent than the norm. Of course, a credit history of prompt payments is expected. However, applicants who have incidents in their records of unsatisfactory credit, but have recently (during the last 1 1/2 - 2 years) been able to demonstrate satisfactory payment records, are requested to provide written explanations of their past problems. Also, credit problems stemming from instances such as an unanticipated layoff or illness do not necessarily spell rejection for the applicant. We understand that an interruption of, or an unusual demand on, income sometimes affects a person of low or moderate income more quickly and seriously than those of higher income.

Sweat equity is also recognized on a case-by-case basis as being equivalent to a cash investment in rehabilitated property. It is important that the individual applying for this credit have the skills necessary to perform the work in a craftsman-like manner, and proper permits must have been issued when appropriate.

Not-for-profit developers are also encouraged to participate in the CRP. The bank is willing to make loans on a nonrecourse basis to organizations that demonstrate they are qualified to perform in this capacity.

For loans made under the CRP, appraisals are performed only by those experienced in appraising properties in the targeted neighborhoods.

Besides developing specialized lending procedures for use under the CRP the bank also included in its overall effort the development of low-cost checking and savings account products. Boatmen's "Basic Checking" account is designed to give low- to moderate- income individuals a way to pay their major monthly obligations without having to resort to purchasing more expensive money orders. The account requires no minimum balance, and customers are allowed to write eight free checks per month. In addition, Boatmen's began allowing noncustomers as well as customers to cash all government checks in amounts of $400 or less at no charge, provided the payee is present and has proper identification.

1989 Demonstration Program

In April 1989, Boatmen's Bank, The Federal National Mortgage Insurance Company (FNMA), and General Electric Mortgage Insurance Company (GEMCO) introduced a new pilot program in St. Louis designed to provide home ownership opportunities to low- to moderate- income borrowers. Four other cities have been included in this demonstration program, Chicago, Cleveland, Cincinnati and Indianapolis. Boatmen's is the participating lender in St. Louis and received a $5,000,000 commitment from FNMA who will purchase the loans during the next year.

The Home Lending Program encompasses several unique features that will benefit low- to moderate- income borrowers. They include:

- A more liberal debt to income ratio. On 95% loans, the mortgage loan ratio is increased to a maximum of 33% of gross income from the standard of 28%. The total debt ratio is 38% from 36%.

- If borrowers have demonstrated an ability to save the 5% down payment, the normal 2 month's liquidity reserve (2 monthly mortgage payments) is waived.

- It is recognized that many of the borrowers will not have a traditional credit history and their credit worthiness may need to be reconstructed from rental history, utility bills, etc.

- The inner city housing stock is recognized to be "different" from suburban housing and represents affordable and decent housing alternatives to qualified borrowers.

- Secondary income is considered based on the length and regularity of all income sources.

The program targets low- to moderate- income neighborhoods and individuals whose income is considered to be low to moderate. Long term (15 or 30 years), fixed rate, fully amortized loans are available.

Homes needing rehabilitation may also be included in the program with property appraisals made based on the after rehab value. Additional assistance is available to these borrowers. The assistance includes:

- Providing the borrower with a list of pre-qualified contractors that are skilled in rehabilitation.
- Property inspections before, during and after completion of the renovation.
- Referral to municipal agencies who assist buyers with planning, inspections, grants etc.
- Access to credit and home maintenance counseling programs.

Benefits of the CRP

The Boatmen's Community Reinvestment Program has been in existence for over 3 years. At the end of 1988, the original goal of making $50 million in real estate loans was exceeded by over 100 percent, with real estate loans made in targeted neighborhoods totaling over $102 million. Nearly half of these loans ($49.7 million) were made for the acquisition and/or rehabilitation and improvement of one- to four- family properties, the vast majority of which are owner-occupied.

Although loan officers often need to devote more attention to processing CRP loans, these loans are profitable. Delinquency ratios for this program, contradicting popular myths about low- to moderate- income lending, have been comparable for CRP-related loans with those associated with our more "conventional" portfolio. Although these loans are not well-aged, it is believed that sufficient time has elapsed to indicate no significant additional credit risk in this portfolio. At the end of 1988, none of the few loans classified as delinquent were past due for more than 30 days. Moreover, default has yet to occur on any CRP mortgage loan.

The success of Boatmen's Community Reinvestment Program cannot be measured in dollars alone. Community outreach associated with the program has earned the respect and trust of St. Louis city and community leaders at all levels. Recently one city official, commenting on Boatmen's CRP, wrote, "The homeowners, neighborhood groups, developers, and the Community Development Agency (of St. Louis city) have all found your program and your commitment to the city to be an example of corporate citizenship at its very best."

Recognition has also been achieved on a national level. An officer of one of our federal regulatory organizations wrote, referring to Boatmen's

Community Reinvestment Program, that "it is certainly an enlightened approach for a financial institution to take. It serves as an excellent example of what lenders should and can do to meet their corporate commitment to the communities they serve."

Conclusion

Meeting the needs of the community is what CRA compliance is all about. But it takes more than simple compliance with the letter of the law. At Boatmen's, a strong emphasis is placed on striving to comply with the "spirit" of the law's requirements. In the dynamic environment of our urban area, we continue to reach out and maintain a constant dialogue with our participating neighborhood organizations as well as with city, county and state housing officials. Internal training is an integral part of this effort as we build on our staff's knowledge of the CRP's special products.

The many lines of communication that have been established are a most important part of Boatmen's community reinvestment effort. Anticipating the needs of our community and customers has eliminated many problems before they had a chance to become obstacles.

POSITIVE INCENTIVES

Senator **Bond**. Mr. Brown, I'd like to have your comments and maybe Mr. Fishbein's on Mr. Kolesar's suggestion that we have some positive incentives, some carrots, as well as the sticks for performance under the CRA. He suggested exception from risk-based capitalization requirements, exemption from application stage CRA challenge, and maybe even a sticker on the door or something that shows that this has been an A-1 bank.

How would you view that kind of positive incentive?

Mr. **Brown**. I think that's an excellent question. I think if you disclose the CRA examination reports or the CRA assessments by the agencies, if those assessments have good substantive information that's credible in them and provide a good analysis of the institution's performance, and if an institution, having gone through that process, receives a good assessment, I think that disclosure of that will in and of itself be very beneficial to the institution.

As I indicated in my testimony, it should be used by institutional investors or public officials in placing public deposits. It's additional information they can use if there's some type of social performance that they factor in their investment decisions on where to place their funds.

So I think it's important to keep that in mind, that disclosure of good assessments will work through the marketplace to reward institutions that have good performance.

It's just that the assessments and the information in them has to be credible. Otherwise, people aren't going to use it. That's one thing and probably in the long run the most important facet because in many ways it is relying on the marketplace. It's just providing information on social performance into the marketplace where it's lacking now.

Second, I think there are some other more tangible types of incentives that could be provided. I think Jack Kolesar's idea of an exemption from risk-based capital requirements makes a lot of sense because after all it's true that those requirements were implemented primarily for safety and soundness reasons, but they have a very powerful credit allocation side effect and I think the agencies are somewhat oblivious to that and I think it's appropriate for the members of this committee to be very sensitive to that, and I think that some of those side effects will be very perverse unless they are corrected.

Under those standards there an 8 percent requirement for small business loans. There's a 4-percent requirement for standard mortgage loans, and a 2-percent requirement for securitized mortgage loans. So in a sense, an institution there has a strong incentive to provide the most standardized, readily salable mortgages which cuts against the grain of community reinvestment initiatives, or say small business funding. It would penalize a bank like Jack Kolesar's bank that specializes in these activities. And yet the track record in terms of the loan losses on those loans suggests that they don't really warrant a higher capital behind them. So that's one thing.

Another possibility would be payment of interest on reserves in some fashion that would reward banks for good performance. The banking industry has long sought the payment of interest on reserves feeling that it's in a sense a tax on them, the fact that they are not paid interest, and I think that here is another way in which their performance could be rewarded.

I think also that the idea of characterizing a whittling away of participation rights, this idea that a bank with a good CRA rating would be immunized from protest, I think that is not really a proper incentive. That we would not support because our feeling is that it would destroy the safety net concept of the ability to protest because there are circumstances when the agencies' evaluations may not be proper and they should be challenged. In addition, there are tremendous practical reasons for leaving the full rights of protest alive because in many cases the CRA examinations become very dated. The Comptroller of the Currency examines many banks now only once every 6 or 7 years. So they will become stale. So we just cannot accept that type of idea. But for the most part, I think they are useful suggestions.

Senator BOND. Mr. Fishbein, I'd appreciate your response to those questions.

Mr. FISHBEIN. Thank you, Senator Bond.

I would like to respond. Before I do, however, I would like to ask the chairman if I could submit some additional attachments into the record.

Senator DIXON. Absolutely. They will be in the record.

[Attachments to Mr. Fishbein's statement follow:]

CCC, Attachment 1

The activist and the bank president. *Willie Lomax, left, and Robert Teresko struck a deal that helps the poor and makes a profit*

A housing program that really works

Bankers hate it, but an anti-redlining law helps the poor and costs little

Imagine an ideal government initiative. One that helps lower-income Americans own their own homes but does not breed welfare dependency, does not expand bureaucracies or budget deficits and does not hurt business or the economy. Such a policy actually exists. It is called the Community Reinvestment Act (CRA). Passed in 1977, CRA says banks have an "affirmative obligation" to lend in lower-income neighborhoods, though there are no firm lending quotas set in the statute and regulators must determine for themselves what is reasonable. In the places where it has been seriously applied and enforced, it has worked with surprising effectiveness. Though by no means a complete solution to the low-income housing crisis, CRA has helped neighborhoods turn around and thousands of lower-income people discover homeownership, the main vehicle by which American families expand their wealth.

The law was ignored or undermined by key officials for years, but that could be changing. Housing Secretary Jack Kemp seems sympathetic to the law, and the Federal Reserve Board, long resistant to tough CRA enforcement, is showing signs of a new willingness to crack down on noncooperative lenders. Last week, the Fed rejected the application of Continental Bank Corporation to purchase a tiny Arizona bank on the ground that Continental had a poor track record lending to lower-income customers. The problem for CRA, though, is that banks still hate the law, and it is not clear that the apparently invigorated Fed policy will spread to other bank regulators at the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board and at the Office of the Comptroller of the Currency.

Newfound safety. The beneficiaries of CRA include people like Irene Wells. The 44-year-old nurse used to live in a North Philadelphia public-housing project where the elevator seldom worked. So she would come home from her night shift at a nursing home and trudge up 17 flights of dark and filthy stairs to her $86-a-month apartment. "I was afraid to go home sometimes," she says. Today Wells and her mother own their own modest row house, purchased with the help of a community group called ACORN and a $17,000 CRA mortgage from Fidelity Bank of Philadelphia. Wells feels safer in her new home, and she and her mother happily pay the $159-a-month mortgage.

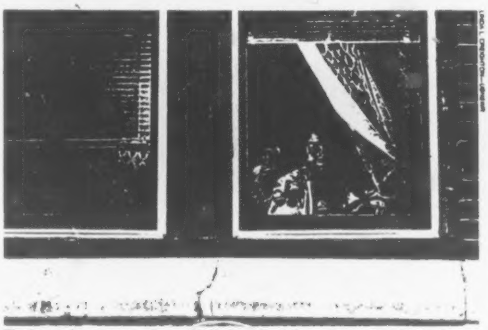
The law had its genesis in a raging controversy in the 1960s and 1970s over redlining, the unwillingness of some banks and thrifts to make loans in lower-

Black and white disparities

10 metro areas with the highest ratio of black-to-white loan rejections

	Black rejection rate	White rejection rate	Black-white rejection ratio
1. Milwaukee	24.2%	6.2%	3.90:1
2. Pittsburgh	31.2%	8.2%	3.80:1
3. Cleveland	31.4%	8.4%	3.74:1
4. Chicago	27.6%	7.6%	3.63:1
5. Detroit	32.5%	9.1%	3.57:1
6. Norfolk–Virginia Beach–Newport News	26.5%	[illegible]%	3.44:1
7. Charlotte–Gastonia, N.C.–Rock Hill, S.C.	26.1%	8.0%	3.26:1
8. Indianapolis	27.9%	8.7%	3.21:1
9. Baltimore	24.2%	7.6%	3.18:1
10. Memphis–Ark.–Miss.	22.2%	7.3%	3.04:1
U.S. average	23.7%	11.1%	2.14:1

USN&WR—Basic data: Atlanta Journal and Constitution, from Federal Home Loan Bank Board data



The happy homeowner. *Irene Wells benefited from the anti-redlining law*

income minority neighborhoods. Though CRA has stopped blatant redlining, discriminatory lending patterns have not disappeared. The *Atlanta Journal and Constitution* reported last month that a study of 10 million mortgage applications showed that even at similar income levels blacks are rejected strikingly more often than whites when they apply for home loans.

With federal regulators long unwilling to put their muscle behind CRA, community groups have taken up the fight themselves. The law lets them challenge the applications that banks must submit to federal regulators for permission to expand their operations. Thanks to such challenges, the amount of capital banks set aside for lower-income lending has grown from about $185 million in 1984 to over $1.229 billion last year.

Bank lending under CRA itself cannot bring back many blighted neighborhoods. But those loans have helped stretch ever scarcer housing subsidies, and, prodded by the law, bankers have uncovered profitable opportunities in places they had previously written off. In the summer of 1987, black activist Willie Lomax and white bank president Robert Teresko found themselves in a shouting match in the lobby of Teresko's Beverly Bank, on Chicago's South Side. The bank wanted to build a branch in the suburbs. Lomax's community group, the Chicago Roseland Coalition for Community Control (CRCCC), wanted more loans made in the nearby black neighborhood of Roseland, where the bank draws many depositors. "We were in front of the customers," Lomax recalls with a chuckle, "and he was yelling, 'Why are you giving me a rough time?' and 'I don't appreciate this!' "

No job, no loan. Eventually, Lomax and Teresko signed a CRA agreement setting aside $20 million (10 percent of the bank's assets) for community lending and allowing the bank to build its suburban branch. CRCCC and other Chicago nonprofits help administer the program, and loans made so far are doing fine. "We're very pleased with the relationship," says Teresko. "It's good for business and for our visibility." The effort, says Lomax, is "not welfare, not a giveaway. If somebody doesn't have a job they can't get a loan. This is good, clean business practice."

For all the good CRA agreements have done, bankers still generally resent being pressed into them. Privately, they point out that nonprofit groups are not immune to corruption and hidden agendas. Yet CRA has avoided scandals, in part because banks can often pick the group with whom they will work. Some of their outrage has also subsided a bit as bankers have found their CRA loans making a small profit, or at least breaking even. CRA loans have high paperwork costs, but their default rate appears to be as good as or better than that of conventional loans. And community organizers argue that they would not have to bring protests if federal bank regulators would enforce the CRA law as Congress intended.

Government and private studies have repeatedly found that regulators give enforcement of CRA and other consumer-protection laws low priority, while auditors who concentrated on consumer issues were found to have limited potential for career advancement. Moreover, the agencies avoid using CRA's full authority to crack down on uncooperative banks and thrifts. Regulators have received over 40,000 expansion applications since 1978. They denied only nine, including the Continental application, on the grounds that the banks practiced discriminatory lending. The regulators say they prefer behind-the-scenes pressure to outright penalties, but another explanation for this permissive record is grade inflation. Every year, 97 percent to 99 percent of banks receive passing marks on their CRA examinations. "Regulators seem to think that we're all living in Lake Wobegon," remarked former Senator William Proxmire (D-Wis.), CRA's chief sponsor last year. "Like the children of the fictional village, U.S. lenders are all above average."

Black and white similarities

10 metro areas with the closest ratio of black-to-white loan rejections

	Black rejection rate	White rejection rate	Black-white rejection ratio
1. Portland, Oreg.	17.5%	15.2%	1.15:1
2. Anaheim-Santa Ana, Calif.	23.3%	16.7%	1.40:1
3. Middlesex-Somerset-Hunterdon, N.J.	21.9%	14.9%	1.47:1
4. Nassau-Suffolk, N.Y.	14.5%	9.0%	1.61:1
5. Riverside-San Bernardino, Calif.	27.4%	16.7%	1.64:1
6. Miami-Hialeah	[illegible]	17.3%	1.65:1
7. Salt Lake City-Ogden	16.3%	9.7%	1.68:1
8. Oakland	23.2%	13.6%	1.71:1
9. San Diego	36.0%	21.0%	1.71:1
10. Bergen-Passaic, N.J.	11.0%	6.4%	1.72:1
U.S. average	23.7%	11.1%	2.14:1

USN&WR—Basic data: Atlanta Journal and Constitution, from Federal Home Loan Bank Board data

Community groups want the grading system stiffened and the grades made public. Regulators such as FDIC Chairman L. William Seidman claim public disclosure would be "counterproductive" and would risk causing public panic—a run on badly rated banks. Evidence suggests, however, that disclosing CRA ratings does not necessarily threaten bank safety. Last spring, publication of a "less than satisfactory" rating (the bottom 2 percent of all banks) for Comerica Bank-Detroit prompted Michigan authorities to insist that Comerica develop a detailed CRA lending plan with community groups as a condition of approving a proposed acquisition. Other Detroit lenders soon followed suit, and there was no bank run.

An ambitious attempt to fix the problems with CRA died in Congress last fall and could be revived and passed in this session, especially if Kemp backs reform. In an interview last week, he strongly rebuked banks for discriminatory lending and said he would like to end the practice by beefing up CRA enforcement and by making thrift institutions that get federal bailouts invest in depressed areas. But he will have to convince President Bush and others in the administration that this is the right approach. Bush is philosophically against regulation, but he is also squeezed between the need for low-income housing and the massive budget deficits. As he feels more pressure, CRA could begin to look better to him. ■

by Paul Glastris with Scott Minerbrook
in Philadelphia

CCC, Attachment 2

doesn't leave much to secure meaningful reduction: other big programs, such as Medicare and farm subsidies, could be hit in a Bush administration.

If Congress balks at the cuts he wants, Bush will push for a line-item veto. That means he would be able to delete any specific expenditure in an overall appropriations bill. Congress will almost certainly refuse to give a new president that authority. Many mainstream economists believe, therefore, that as president Bush would have to accept a tax increase to cut the deficit. Bush advisers say privately that he probably would agree to some excise taxes—on oil, perhaps—as a compromise with Congress. Washington's "bipartisan economic commission" may provide an escape route next year when it registers its inevitable call for spending cuts and tax hikes. Bush "does not believe that there is never a time in the world when a tax increase would be necessary," says one adviser. He adds, however, that he does not believe Bush would agree to tax increases as early as next year.

'Wiggle room': The deficit, no matter who wins, will haunt the next president. No major assault on drugs or AIDS research is possible until government can spend more money. Says former Congressional Budget Office director Rudolph Penner, "It may be the [next] president won't make that much difference. You may have somewhat different spending cuts . . . but the basic policy thrust would be similar. There's just not that much wiggle room left."

On the surface, the economy seems to be cutting in Bush's favor. There may simply be too many good-news numbers around for Dukakis to make a cogent case for change. Unemployment in the United States last week ticked down to 5.4 percent, the lowest level in 14 years. The Democrats, however, believe there is a pervasive sense of unease about the country's economic health that Dukakis can exploit. According to polls, voters worry that if the deficits are not dealt with promptly, they could sap the nation's economic strength.

According to a formula devised by Ray Fair, a Yale University economist, presidential elections can be predicted with impressive accuracy by looking almost exclusively at the health of the economy. Fair cranked GNP and inflation data for the last 18 election cycles into a computer recently, and in 15 of them the computer spat out the correct winner. This time it's spitting out B-u-s-h. But be forewarned: one of three times it erred was in rerunning the 1960 election, when a challenger from Massachusetts promising change upset a sitting vice president preaching continuity.

BILL POWELL *with* RICH THOMAS *and*
ANN MCDANIEL *in Washington and*
CAROLYN FRIDAY *in New York*

ROB NELSON—PICTURES GROUP

A pattern of discrimination that touched even black officials: *Lomax in front of property*

The Return of 'Redlining'

An Atlanta bank exposé revives a tindery issue

The Sunday, May 1, edition of The Atlanta Journal and Constitution led off with a shocker. It was the beginning of a series of articles accusing Atlanta's banks of discriminating against blacks. According to the painstaking analysis of computer data provided by the banks themselves, lenders were five times more likely to give mortgage and home-improvement loans to whites than to blacks. The paper quoted an Atlanta mayoral candidate, Fulton County Commission chairman Michael Lomax, who had to approach three banks before he was able to get a $115,000 home-improvement loan. Lomax asked, "If I, a powerful black elected official, can't get a loan, what black person can?"

The series hit Atlantans hard. Atlanta City Council president Marvin Arrington recalls that when he read the first article on Sunday, "I sat there with my head in my hands, with tears running out of my eyes." The news was especially jarring since Atlanta has built an image as a bastion of good race relations and opportunity for blacks. The timing couldn't be worse. Atlanta hopes to showcase its achievements during the Democratic convention there in July. The series also underlined the fact that "redlining"—denying loans in ethnic neighborhoods—is alive and well, and not just in Atlanta. Similar investigative methods used for the articles have turned up inequities in Chicago, Washington, D.C., Denver and Baltimore. A hot topic in the 1960s and '70s, the issue of redlining had largely died down thanks to federal action and bank efforts to promote minority interests. Despite that progress, a pattern of discrimination persists—a subtle, institutional discrimination that shuts the teller's window on blacks.

Bankers generally deny that racial redlining exists. They say the problems are economic. "Banks are not worried about color of skin," says George Stone, first deputy commissioner of the Chicago Department of Housing. "They're worried about capacity to pay back loans." Still, some lenders concede the result is unfair—and damaging. Lee Sessions, executive vice president of C&S bank, said, "Anything that is *perceived* as a problem is a problem."

Few defaults: The next step is Atlanta's to take: the city has pledged to work with banks to develop better investment in the predominantly black south side of town. If that doesn't work, boycotts could result. City leaders say lawsuits could be in the works and that Atlanta might even pull funds from banks with bad investment records. Arrington hopes that won't be necessary. "We're not here to beat up on anybody," he said at a meeting with bankers. "We're looking for solutions."

It's unclear how much even well-intentioned institutions will be willing to do. Mortgages in some poor urban areas actually have low default rates. But they yield less profit and often require government subsidies to make them work. Still, banks have absorbed much bigger losses on supposedly high-profit ventures like loans to the Third World and to the oil patch. In comparison, equal-opportunity lending looks like a smart investment.

JOHN SCHWARTZ *with* FRANK S. WASHINGTON
in Atlanta

103

CCC, Attachment 3

The Boston Globe 1/11/89

Inequities are cited in Hub mortgages

Preliminary Fed finding is 'racial bias'

By Steven Marantz
Globe Staff

Local banks and thrifts are awarding fewer home mortgage loans in Boston's minority neighborhoods than in white neighborhoods, in part because of a racial lending bias, according to an unpublished study by the Federal Reserve Bank of Boston.

"This racial bias is both statistically and economically significant," the April study by two Federal Reserve officers said. Housing mix, relative purchase and rental prices, turnover rates and the physical condition of neighborhoods are also factors in lending patterns, the study said.

Officials at the Federal Reserve Bank of Boston yesterday described the study as inconclusive while saying that they are studying home mortgage lending patterns by local banks and thrifts. One of the study's authors, Constance R. Dunham, said in an interview that the study is unpublished because it is a preliminary draft and the conclusions are premature.

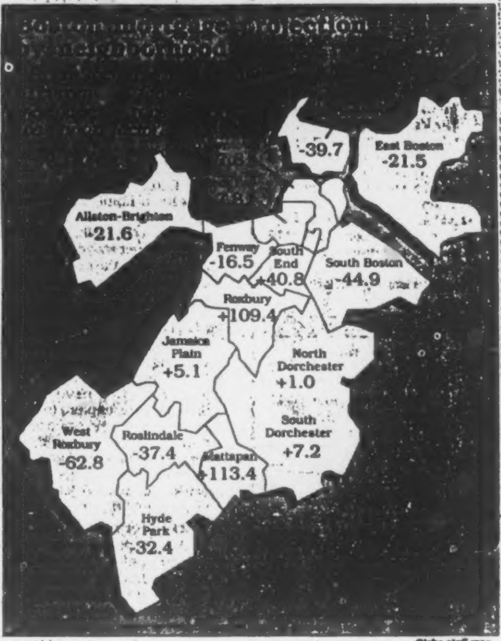
The study, a copy of which was obtained by The Boston Globe, concludes from statistical analysis that if banks and thrifts competed with equal aggressiveness in white and minority neighborhoods, they would make "far fewer loans in predominantly white neighborhoods . . . and would have more than doubled their actual number of mortgage loans in the predominantly black areas of Mattapan/Franklin Park and Roxbury."

Disclosure of the study comes as the Boston Redevelopment Authority is set to approve the hiring of University of Minnesota economist Charles Finn to investigate the lending patterns of the city's financial institutions.

Dunham said that she is continuing to study local lending patterns but declined to say why the study was initiated.

"I want to make it very clear that the reason the draft wasn't published is that I wanted to do

MORTGAGES, Page 12


-39.7
East Boston
-21.5
Allston-Brighton
+21.6
Fenway
-16.5
South End
+40.8
South Boston
-44.9
Roxbury
+109.4
Jamaica Plain
+5.1
North Dorchester
+1.0
South Dorchester
+7.2
West Roxbury
-62.8
Roslindale
-37.4
Mattapan
+113.4
Hyde Park
-32.4

Globe staff map

■ MORTGAGES

Continued from Page 1

subsequent work on the topic," said Dunham, an assistant vice president and economist. "I'm now doing work that would show that there could be reasons other than racial discrimination to explain the mortgage lending patterns.

"Therefore, it is erroneous to conclude from the preliminary draft that racial discrimination explains the patterns that I talk about in the paper. ... I don't know if the lending patterns will be the same as I described in that paper. I don't know if they are indicative of what is going on or if they are misleading."

Asked if her initial conclusions were faulty, Dunham said, "I haven't gotten the answer yet." Pressed for elaboration, Dunham said that she is studying supplemental lending data that she did not use in her previous work.

The other author, William J. Spring, vice president and community affairs officer, referred questions to Dunham.

Dunham, who has worked for the Federal Reserve since 1979, has reviewed bank applications protested under the Community Reinvestment Act and studied the impact of interstate banking activities on lending.

Spring, who has been at the Federal Reserve since 1981, also has worked on Community Reinvestment Act issues. The act, passed in 1977, requires financial institutions to serve the credit needs of all areas where they collect deposits. The Federal Reserve monitors compliance with the act.

The study, titled "Expanding the Potential of the Community Reinvestment Act: The Case for Affordable Housing in Boston," was scheduled to be published in the May/June 1988 issue of the New England Economic Review, a publication of the Federal Reserve Bank of Boston, as indicated by a footnote on its first page.

Dunham, who wrote the footnote, said the article did not appear "because I didn't feel it was ready yet."

However, Alicia H. Munnell, a senior vice president and director of the research department, said that Dunham footnoted the article as she did because she believed it was ready for publication.

"She thought she was ready to publish," said Munnell. "It's a natural reaction that we all have when we finish a project that we've worked on for a long time."

Munnell said she and Lynn E. Brown, another Fed vice president, made the initial decision not to publish the study because they believed she needed more support for her conclusions.

A source within the Federal Reserve said the final decision was made by Frank Morris, who retired as president at the end of 1988 and was replaced by Richard Syron.

The source said Morris wanted the racial component of the study more thoroughly researched before publication but intended to publish it if the findings held up. Morris wanted an expanded study to focus on individual banks and on private mortgage companies, the source said.

Morris was cautious because there was little or no precedent for analyzing lending patterns using home mortgage data, the source said. "He didn't want to drop it as a bomb, but to let the banks know first and then publish," said the source.

But Finn has developed an analytical method that turned up findings of racial bias in lending in Atlanta and Detroit in two 1988 studies and that is currently being applied in several cities.

Reform examined

Another part of the study, regarding reform of the Community Reinvestment Act, was directed by Morris as an internal memo to Alan Greenspan, chairman of the Federal Reserve Board, and will not be published, the source said.

The study analyzes mortgage figures in 16 neighborhoods for 1985 and draws upon statistics from a five-year period, 1981-85, to factor in demand variables such as median purchase and rental prices, housing mix, historical turnover rates and physical condition of the neighborhoods.

"Even after taking into consideration variation in demand, lending bias appears to be a significant factor explaining why fewer than expected one-to-four family mortgage loans are made by banks and thrifts in minority neighborhoods in Boston," the study says.

One set of figures shows that if race were not a factor in lending in mortgages for one- to four-family houses, there would be a 113.4 percent increase in mortgages in Mattapan/Franklin and a 109.4 percent increase in Roxbury.

The same table indicates that mortgage lending would decrease by 62.8 percent in West Roxbury, 44.9 percent in South Boston, 39.7 percent in Charlestown, 37.4 percent in Roslindale and 32.4 percent in Hyde Park.

"Thus, long after the passage of the CRA, banks and thrifts continue to compete more aggressively in white neighborhoods in Boston and leave the minority neighborhoods to the mortgage companies," the study says. "Boston has become a city with significant unmet credit needs for affordable housing, and continues as a city with signficant racial lending bias."

The study asserts that unmet credit needs underlie an increasingly desperate housing problem in Boston. It shows that between 1983 and 1987, the median price for single-family houses rose from $82,600 to $178,600. Median family income rose from $26,300 in 1981 to $33,200 in 1985.

"Clearly, housing that is produced without subsidies to the costs of finance, rehabilitation, or construction is simply not affordable by large segments of the population, buyers and renters alike," the study said.

The study does not cite individual banks, nor does it explore the effect of private mortgage companies on lending patterns.

The study proposes broad revisions in the Community Reinvestment Act's regulatory structure, pointing out that the regulation does not provide for disclosure of lending data that allows for the "assessment of the distribution of loans to the lower-income or minority members of lower-income or minority neighborhoods."

The study recommends that "the definition of 'local community' contained in the regulation and in policy interpretations should be made more specific so that it refers to the credit needs of the population within the defined area – for example, the credit needs of lower-income residents in lower-income neighborhoods."

A spokesman for the Massachusetts Bankers Association, Robert Fichter, said that he could not comment on the study without seeing it but that the subject is a "difficult one to get a hold of."

"I wouldn't say anything until different banks got hold of it and looked at it and compared their data," said Fichter.

Question of publishing

Rep. Thomas M. Finneran (D-Dorchester), chairman of the House Banking Committee, said last week that he wants to know why the report has not been published.

"You wonder if the banks who would have been embarrassed by it squashed it," said Finneran. "The problem from my perspective is that the Federal Reserve did not see fit to share it with anybody. I hate to think that they just engage in academic studies.

"Many people, including myself, have a definitive interest in compliance or noncompliance with the CRA. I'm from Dorchester and Mattapan, and it's fairly well known I'm no great fan of banks. I hate to think a fair number of people out there in Roxbury or Mattapan or Dorchester are being denied because of the color of their skin or the location of property they want to purchase. I would hit the ceiling about that."

City Councilor Bruce C. Bolling (Roxbury) said that if the study's conclusions are true, "then banks are acting unconscionably."

"There is a resurgence going on in the core of Boston that is spreading to the neighborhoods," said Bolling. "For the first time there is a chance to reinvest in Roxbury in a meaningful way. Rather than take advantage of the opportunity, it appears that the major lending institutions have continued to engage in discriminatory lending practices."

Not surprised

Ron Homer, president of the Boston Bank of Commerce, the city's only black-owned bank, said that it was difficult to comment without having read the study but that the findings "are not news to the minority community.

"Banks tend to be similar to all kinds of institutions who tend to invest and deal with the type of people who work within them, and many banks don't have strong associations with the minority community," said Homer. "They certainly don't spend resources trying to promote themselves in the minority community. You just have to walk through the black community to realize that there isn't a lot of investment.

"To the extent that there is a discrepancy, I don't think there is institutional racism, but I think it's people doing business as usual."

Homer said the study's reliance on statistics through 1985 might present a skewed impression because "my sense anecdotally and in general perception is that much positive has happened since 1985."

Lew Finfer, director of the Massachusetts Affordable Housing Alliance, said that he is surprised such a study is being undertaken by an employee of the Federal Reserve Bank of Boston.

"It's startling that such a well-established group would have done that kind of study," said Finfer. "I'd like to know whether it was a legitimate research question or politics that caused them to back off."

Finfer said that his impression is that housing speculators are obtaining loans to buy Roxbury property in the Dudley Street corridor but that residents in the Codman Square, Grove Hall and Franklin Field areas are having difficulty obtaining mortgage and home equity loans.

CCC, Attachment 4

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PAGE 1 SET 14 WITH

STORY 1

ACCESS NUMBER	207421
NEWSPAPER	(c) THE WASHINGTON POST
DAY	TUESDAY
SECTION	FINANCIAL
PAGE	e01
LENGTH	24 INCHES
STORY TYPE	NEWS NATL
DATE	04/25/89
HEADLINE	ATLANTA BANKS PROBED ON REDLINING; U.S. INVESTIGATING ALLEGATIONS OF RACIAL BIAS IN MORTGAGE LENDING
BYLINE	Bill Dedman
CREDIT	Washington Post Staff Writer

START-OF-TEXT

The U.S. Justice Department has notified all 64 banks and savings and loan associations in metropolitan Atlanta that they are under investigation for possible racial discrimination in mortgage lending.

In letters that began arriving yesterday, Justice's Civil Rights Division disclosed the largest investigation ever of redlining -- the refusal to lend on the basis of race or other factors unrelated to creditworthiness. Redlining is forbidden by the Equal Credit Opportunity Act and the Fair Housing Act.

The letters met with sharp denials in the executive suites of Atlanta's banks, which have been buffeted for a year by newspaper articles describing racial disparities in lending patterns.

"We do not discriminate. We do not discriminate. We do not discriminate," said Willis Johnson, spokesman for Trust Company Bank, the third-largest Atlanta-based bank.

The Justice letters, signed by Acting Assistant Attorney General James P. Turner, give the lenders official notice that they are under civil investigation and ask them to make available voluntarily all loan records from the past five years. Officials at a number of banks said yesterday they would cooperate with the inquiry.

Justice also asks for answers to a detailed questionnaire about marketing, branch locations and hours, loan authority, underwriting guidelines, training handbooks, real estate agent contacts, appraisal policies, and lists of employees by name and race.

Fair housing advocates and legal experts welcomed the investigation. The case is the broadest such inquiry since the government settled a suit against the national real estate appraisal associations in the late 1970s.

"It's a significant case," said Stephen M. Dane, a fair housing attorney in Toledo. "I interpret it as a long-overdue but certainly welcome resurgence of interest at the Department of Justice in housing finance discrimination."

Advocates also read between the lines in the letters a rebuke to the four federal bank regulatory agencies: the Federal Reserve Board, Office of the Comptroller of the Currency, Federal Deposit Insurance Corp. and Federal Home Loan Bank Board. Although the bank agencies have reported declines in lender compliance with the Equal Credit Opportunity Act, they have not referred a case of credit discrimination to the Justice Department since 1978.

"It has to be a backhanded slap at the regulatory agencies," said Allen Fishbein, general counsel of the Center for Community Change, a neighborhood-advocacy group based in Washington. "You would think the normal investigation and enforcement process would weed out lawbreaking, but the regulatory agencies have been unable and unwilling to do that."

The four bank agencies said they are cooperating with Justice and see no rebuke.

"We have already said we have not been doing an adequate job enforcing consumer regulations, because of the increase in the number of problem banks. We admit that," said Lee Cross, spokeswoman for the Office of the Comptroller of the Currency, which regulates national banks. "It is possible that we are missing some kinds of discrimination. That concerns us, and we are taking steps to improve enforcement."

The investigation was prompted by articles beginning last May in The Atlanta Journal-Constitution that disclosed a segregated mortgage system in which banks and thrifts made few loans in black areas, even in upper-income black areas, and often made mortgage services less accessible to black home buyers.

Atlanta's largest banks responded to the articles by pooling $77 million for low-interest mortgages primarily in black neighborhoods. A few of the largest banks also changed some policies, such as increasing contacts with black real estate agents. Many smaller institutions reported no changes.

The Justice inquiry, going beyond information available to the newspaper, seeks records of actual loan applications and credit reports on mortgage applicants. If lenders comply with the Justice requests, investigators will be able to compare rejected applications by black home buyers with approved applications by whites.

Also receiving the Justice letter were private mortgage companies affiliated with banks, including Citicorp Mortgage Inc., a subsidiary of Citicorp, America's largest banking company. The Journal-Constitution disclosed in December that Citicorp called on real estate agents only in predominantly white neighborhoods in metropolitan Atlanta. Citicorp officials denied any intentional discrimination and said they had expanded their marketing program.

Atlanta bankers said the Justice investigation was expected but they said they don't fear it.

"We don't feel we have discriminated overtly. I don't think there is a single instance of outright discrimination by any of the larger institutions," said James J. Wallace, director of communications for Fulton Federal Savings Bank, Georgia's largest savings institution. "We went back and reviewed every one of our declined applications. One black applicant had an income of about $50,000 but had nine separate VISA and MasterCard accounts and they were all up to the limit. That's just an example.

"If there was a problem," Wallace said, "it was in the method of obtaining applications. If the real estate brokers don't bring applicants to you based on previous experience, then you have a problem."

Legal experts agreed that a Justice case probably would depend on actual denied applications combined with a pattern of avoiding black neighborhoods.

"The fact that Justice is looking at marketing efforts should cause many lenders around the country to seriously look at their patterns and practices," said Dane, the Toledo attorney, who has handled many fair housing cases.

"Whether they're intending to avoid black neighborhoods, or whether they're merely intending to maximize profits by marketing only to white neighborhoods, the effect is the same," he said.

END OF STORY REACHED

CCC, Attachment 5

Business

Chicago Tribune Tuesday, April 25, 1989

Bank funds pledged for community

By Christine Winter

Two Chicago banks on Monday added to the swelling tallies of funds available for community reinvestment in low- and moderate income neighborhoods.

First Chicago Corp. said it will make $150 million available over the next five years for residential and small-business loans, the largest reinvestment program in the country.

In 1984, First Chicago pledged $100 million, of which $75 million worth of loans were made to finance more than 2,800 housing units and 130 commercial spaces. The remaining $25 million will roll over and be included in Monday's new pledge.

First Chicago officials also said the bank will increase its contributions to community groups for neighborhood development by 25 percent to $500,000 annually.

Continental Bank also announced Monday that it is seeking approval to set up a separate subsidiary designed to allow the bank to participate in community projects it might not otherwise have been able to do under banking regulations—such as taking equity positions in development projects.

Continental said it will fund the new subsidiary, if approved by federal regulators, with $1 million, which will be separate from any of its other community lending programs.

Those include $41 million in programs for individual and multiple apartment rehabilitation projects and a "strong policy of making normal business deals in low- and moderate-income neighborhoods."

In addition, Talman Home Federal Savings & Loan Association, Chicago's largest thrift, on Tuesday is expected to announce its participation in a consortium of lenders to provide mortgages for home buyers in low and moderate income neighborhoods.

At First Chicago, Chairman Barry Sullivan pointed out that community lending is "a business we find attractive."

He added that during the first five years of First Chicago's program, the default rate on community loans was under 1 percent.

Sullivan acknowledged that when the bank made its first community lending commitment in 1984, it was under pressure by neighborhood groups that threatened to protest its acquisition of American National Bank.

He added that there is "no other motivation" this time.

Under the Community Reinvestment Act, the Federal Reserve Board can reject acquisitions by bank holding companies if any of the banks involved do not make adequate investments in their own communities.

"Without the pressure of the American National Bank acquisition; it shows this is a pure program that makes a lot of sense," said Gail Cincotta, executive director of the National Training and Information Center. "We were right five years ago

See Bank, pg. 2

Tribune photo by Walter Kale

On hand Monday for the announcement of First Chicago Corp.'s community reinvestment project are, from left, Sen. Alan Dixon, First Chicago's Barry Sullivan, Gale Cincotta of the National Training and Information Center, and Michael Schubert of the Department of Housing.

Bank

Continued from page 1

when we bet banks they could make money in our neighborhoods."

However, much attention has been placed on community lending programs since the Fed startled the nation's bankers in February by rejecting Continental Bank's application to acquire a small Arizona bank. Federal officials said Continental had not complied with the Community Reinvestment Act. Adding fuel to the fire is the rumor that Congress may include community lending provisions as part of the thrift rescue legislation.

When Continental's acquisition request was rejected—even though its lending program had the support of neighborhood groups—many believed Continental had been caught in the crossfire of a regulatory turf war. But the Fed may have been signaling renewed interest in the reinvestment act as well.

"We were caught up in a communications problem," said Thomas Theobald about Continental's earlier rejection. "It shows, however, that you can't just have a substantial program, you have to have advertising and make it known."

Richard Hartnack, senior vice president at the First National Bank and head of the personal banking group, said the current First Chicago program was already being crafted before that ruling last February.

He added that the Fed's apparent concern is not as significant a factor here as the "good experiences" Chicago banks have had with their programs.

"I think the Continental ruling has had more effect on banks outside of Chicago, which is known for its strong community development programs," he said. "The feeling seems to be if the Fed could go after a Chicago bank, then everybody else better start looking at their programs."

New York State Banking Department CCC, Attachment 6
CRA ASSESSMENT REPORT (OFF-SITE)

FIRST AMERICAN BANK OF NEW YORK ASSESSED NOVEMBER 19, 1987

Pursuant to the provisions of Section 28-b of the Banking Law and Part 76 of the General Regulations of the Banking Board, an assessment was conducted of the First American Bank of New York to evaluate the institution's record of performance in meeting the credit needs of its entire community including low- and moderate-income areas, consistent with the safe and sound operation of the institution.

Scope of the Assessment

The most recent on-site assessment of the institution, conducted by the Banking Department as of December 31, 1986, was reviewed to determine if any areas of noncompliance had been noted. Responses to the 1987 CRA Informational Request were reviewed for accuracy, completeness and relevancy. The 1987 CRA Statement and the most recent State Report of Examination were reviewed to identify any potentially relevant material.

Assessment Summary

Due to the widespread distribution of the bank's branch offices, it has delineated 14 separate communities covering all or part of 15 counties as its service area. Such delineation is made on the basis of proximity to the various branch locations of the institution. This methodology of service area delineation is considered effective for this institution, and does not appear to exclude by design any low- or moderate-income area.

Information concerning the credit needs of the various communities served by the institution is obtained through an extensive network of officer and

Assessment Summary (Cont.)

director involvement with a broad range of business and service associations. A review of the most recent CRA Statement indicated that such involvement existed in each of the 14 communities constituting the institution's service area.

The directorate reviews the CRA Statement and the bank's performance thereunder on an annual basis. The last such performance review and CRA Statement readoption took place on February 24, 1987.

Both print and broadcast media are utilized to advertise the availability of credit services to the general public. The nature of the advertising program varies among communities, based on the advertising outlets available within each individual area.

During the past three years the bank expanded its branch network via the 1984 acquisition of 36 branches from Bankers Trust Company. One branch, which represented a near-duplication of location, was the only office closed during the period.

The bank experienced substantial growth in its loan portfolio in 1986. During the period April 1, 1986 to December 31, 1986, residential mortgage loans increased 103 percent to $134 million, and consumer loans increased some 19 percent to $140 million. The majority of this increase represents loans within the delineated service areas.

Assessment Summary (Cont.)

In addition to increases in the volume of loans to individuals, the bank has also been active in SBA lending, and now has an aggregate portfolio of some $2.7 million in such loans. The institution is also involved in both commercial real estate and residential housing rehabilitation programs in virtually all of the urban areas within its various designated service areas.

Rating

This evaluation was based on the review of the most recent on-site assessment of the institution, as well as information furnished by it to the Banking Department. Based on the information available, there is no indication that any area or group has been denied access to credit services on the basis of economic status. As a result, the continuation of a "Two" rating (on a scale of one to five) appears warranted. A "Two" rating means that the bank has established a satisfactory record of meeting the credit needs of its community.

OFF-SITE CRA ASSESSMENT REPORT

Atlantic Bank of New York Assessed May 22, 1987

Pursuant to Section 76.4 of Part 76 of the General Regulations of the Banking Board, a CRA assessment of Atlantic Bank of New York was conducted, off-site, to determine whether the Institution is in compliance with the technical requirements of the Community Reinvestment Act, and to assign a numerical CRA rating based on a one to five scoring system with "One" being the highest.

Summary:

A review of the Bank's current CRA Statement did not reveal any exceptions to the Rules and Regulations of the Federal regulatory agencies. The delineations of the service areas are judged to be reasonable in that there is no evidence that low-and moderate-income neighborhoods were arbitrarily excluded.

The files of the New York State Banking Department did not contain any exceptions and/or violations which required follow-up or corrective action.

Since the previous CRA assessment, no letters of complaint, protests or other communications of a derogatory nature have been filed with the Community Reinvestment Monitoring Unit of the Banking Department.

A geocoding of Atlantic Bank's mortgage loan originations in 1986 revealed that approximately 68% of the loans were for properties located within the Bank's delineated service areas. Of the total originations, 15% of the number of loans and 21% of the dollar amount were for properties located in low- to moderate-income census tracts (census tracts where the median family income is less than 80% of the median family for the Standard Metropolitan Statistical Area in which the census tracts are located).

The Bank is negotiating with the City of New York for the development of a "World Fur Center" in College Point Industrial Park in Queens, similar to the Metropolitan New York Flower Market which Atlantic Bank developed in 1985. A committment has also been made for a 50% participation in a building loan for total rehabilitation of 71 residential units located in Harlem.

Rating:

Inasmuch as no uncorrected violations or adverse comments are in evidence, the CRA rating of "One" (1), which was assigned to Atlantic Bank of New York for 1987, is continued for 1988.

Institutions in this rating category are judged to have a excellent record of CRA performance.

July 30, 1987

BEVERLY BANK
CHICAGO, ILLINOIS

Community Reinvestment Act
Summary Assessment Comment

A review of the subject bank's performance relative to the Community Reinvestment Act (CRA) was conducted as of May 18, 1987. The bank is very active in student loan programs and consumer lending. The majority of the bank's loan extensions are within the delineated community, including several commercial loans to local small businesses. Although it was noted the volume of traditional real estate mortgages and home improvement loans made by the bank since the last examination was low, the bank's new home equity loan program is being marketed in the community and reportedly is being used as a substitute for more traditional real estate loans. The bank appears to be addressing the credit needs of its delineated community in a generally satisfactory manner.

Mr. **Fishbein**. I essentially agree with Jonathan's comments. The idea of incentives should certainly be explored. Looking at risk-based capital requirements which do seem to have a disadvantageous effect on non-standardized loans is a very important one, as well as looking at interest on reserves as an incentive.

However, it really needs to be emphasized that those kinds of incentives work only when you have a meaningful evaluation system and there is confidence in that evaluation system. That still has to be the starting point. We ought to be exploring incentive mechanisms, but the first step is getting these exams to work.

You talked about some kind of sticker idea and I immediately associated that with something that community groups in Camden, NJ do. They have a number of agreements with banks in those cities and when the banks make loans in low and moderate income areas, such as housing loans, they put stickers of those banks right on the windows of those houses. Further, they take lenders around and the lenders start saying, "Hey, that's my competitor's sticker over there and how come mine isn't there?" And the community leaders say, "Well, start making loans in the neighborhood and we'll be glad to have your stickers on the windows."

So I think there are ways through the normal market forces to create the kind of competition. As Jonathan said, that the disclosure of exam reports would create that kind of competition as institutions would try to outdo each other with more creative responses to local community credit needs.

Senator **Bond**. I'd have to say that I would think that that sticker on the door or the window is a lot more obvious than any exam report. I think that's an excellent idea and a very interesting suggestion.

I wanted to go back to Mr. Brown just for one point. If you wouldn't cut off the ability to make protests for an institution which had achieved a high CRA standard. Are you concerned about groups which may file a challenge in order to encourage a community donation to their organization, and how would you deal with that?

COMMUNITY GROUPS MAY FILE A CHALLENGE

Mr. **Brown**. I guess there are almost two separate issues there. One is the question of what about if an institution that has a good CRA rating from the agencies and should it be subject to protest. I think that if the ratings are done well, if they have credibility, that it's very unlikely that it will be protested as long as the exam and rating were reasonably current because any neighborhood group would have a tremendous burden to overcome to get the agencies to reverse that decision and actually deny an application or hold it up.

So I think that problem, in terms of protesting institutions with good records, should take care of it.

The second question you raised is in a sense, are people filing protests without regard to the performance of the institutions just simply to get some type of a contribution.

I am not aware of any situations where that really has occurred. Mr. Fishbein can probably elaborate in a little more detail on that than I can, but I think that is a hypothetical situation that has just not arisen. I think that the agencies have ample powers to deal with that situation. If they feel that a protest is spurious, then they can dismiss it and give it short shrift.

Senator **Bond**. Let me ask you about the converse of that. Do you think that there are institutions that make contributions to community organizations, the institution not having such a good financial record, may make a contribution in order to avoid a protest?

Mr. **Brown**. I'm not aware of where that has happened. I know financial institutions make a lot of contributions for a lot of reasons, which I'm sure members of Congress are aware of, but I don't believe that that is a problem that has in any way affected CRA implementation.

Senator **Bond**. Mr. Fishbein.

Mr. **Fishbein**. It is a very important issue because that does get raised from time to time. And I have not seen evidence that community groups have brought protests to receive contributions.

Senator **Bond**. What about the converse of contributions being made to avoid protests?

Mr. **Fishbein**. Well, I cannot speak for the industry. However, in terms of CRA evaluations by the agencies, of course, contributions should not be taken into account in evaluating their record because CRA deals with how well they are serving credit needs, not how well they are making charitable contributions to their local community.

Senator **Bond**. Let me ask your comments generally across the board on whether you think that CRA or something like it should apply to other institutions beyond banks and savings institutions. Mr. Conville, let's start on this side.

Mr. **Conville**. I am in a business where I compete on both the loan side and deposit side with organizations that are not subject to the same amount of regulation. I personally am an advocate of an "even playing field" in all regards. So I would personally feel that way.

Senator **Bond**. Mr. Kolesar.

Mr. **Kolesar**. I absolutely concur with that. I think now that we're all in each other's business, if you will, on the profit-making side, we ought to all be playing by the same set of rules in terms of public responsibility.

Senator **Bond**. Mr. Fishbein.

Mr. **Fishbein**. I support the concept that all financial service institutions that take deposits have a responsibility to local communities. However, at the same time we differentiate between depository institutions that are backed up by the Federal Government with deposit insurance and nondepository institutions. The reinvestment requirement of necessity would have to be different for those nondepositories than for banks and savings and loans.

Senator **Bond**. Mr. Brown.

Mr. **Brown**. I believe that last point is essential and that is that if CRA is to be extended or something like CRA to other financial institutions, it should be separate legislation and Congress should think carefully about what it is that they would like to see the other institutions do because even though they do compete with the banks either on the loan side or the deposit side, many of them have very different functions and what you can expect from them is very different. They are subject to a different regulatory apparatus and have different functions in the financial marketplace.

A good example are mutual funds, in particular money market mutual funds, may be one of the toughest competitors for banking institutions. And yet to ask money market mutual funds, which in a sense their assets are limited to very liquid and short-term high-grade securities, to ask them to make a lot of community reinvestment type investments is not realistic because that's just incompatible with their function.

So I would hate to see CRA reform legislation dealing with banks and depository institutions held up until such time as all the nuances of extending this concept to other areas are worked out. I think that would be very unfortunate. And there are also, at least on the House side, many jurisdictional issues involved as everybody discovered last year.

Senator BOND. Mr. Chairman, we have a very clear-cut divergence of opinion very articulately stated and so I now turn it back to you.

Senator DIXON. Well, I thank you very much. I think your questioning was very, very useful.

I think in particular the idea of the positive incentives is something that we may consider very carefully in the subcommittee and I think everything that's been said is useful in that regard.

Let me get back to something the chair would like to do in another hearing and it comes through so clearly in all these hearings about your genuine concerns all across the spectrum of different opinions about how well this is being done in the agencies that are looking at the community problems.

Mr. Fishbein, you said four agencies, and would you name them—FDIC——

Mr. FISHBEIN. The Comptroller of the Currency, the Federal Reserve Board and the Federal Home Loan Bank Board for as long as it exists.

Senator DIXON. Now I don't want to embarrass you and if you don't want to answer this I'm not trying to put anybody on the spot, but I got the impression from one of you—I think it was you, Mr. Fishbein—that there's various degrees of quality of performance in these four agencies. Well, at least you said only one, FDIC, would give you any information at all. I saw the demonstrative evidence. It didn't impress me that you got much there, but you at least got volume I suppose.

But is there a difference in how well these four agencies perform that task, their CRA task?

AGENCY ENFORCEMENT

Mr. FISHBEIN. One of the most difficult areas for groups like my own that try to monitor agency enforcement is to keep track of the four different agencies in CRA enforcement because over the 12 years of CRA it changes. One year one agency will appear to be a little bit better than the other. Another year a second agency will come forward. But the fact is that there really are four slightly different approaches to enforcement, four slightly different allocations of resources to enforcement, four different philosophies about whether applications ought to be denied if strong CRA issues are involved. These policies change from time to time. I know that has been a concern to banks and financial institutions because some of them—for example, subsidiary banks of bank holding companies where a bank holding company may have one bank regulated by the Comptroller and another one by the FDIC—may find that the different agencies have slightly different approaches to the examination process. It is very difficult for them to develop a uniform enforcement system to put themselves in preparation for these exams.

Senator DIXON. Well, that's very useful. You're suggesting I think two things. First of all, that different ones of these four do a better job in any given year; and secondly, I think you're saying there isn't any uniformity of standards at all between the four.

Mr. FISHBEIN. Well, there is some uniformity. There is certainly a common set of regulations. They just issued a joint policy statement. In a general way, they are supposed to look at the same criteria. But the levels of training that they provide for their examiners differs. The Federal Reserve Board has specialized consumer compliance examiners that conduct CRA exams, whereas the three other agencies use their safety and soundness examiners to conduct CRA exams. So the quality of training and expertise varies between these agencies.

Not only that—a number of years ago I served on the Federal Reserve Board Consumer Advisory Council. While a member, I took part in a study, which Chairman Volcker asked the council to take a look at, concerning the Fed's enforcement of CRA. I served on a committee of ten members of the council, including lenders, community representatives like myself, and academics. We toured some of the Federal Reserve banks. In speaking to examiners at the banks and with the supervisory staff, we found that there were differences in philosophy and approach between the different Reserve banks, not just between the agencies but between individual Reserve banks. As we go to an era of increasing regionalization and nationalization in banking it must be very frustrating to banks to be supervised and come under the different philosophies of these different Reserve banks.

Senator DIXON. Now let me ask you this. Is there a key player at each one of these agencies that you would name as the person who makes policy more than any other person? That is to say, who at FDIC is really the person that is the key person on CRA stuff if we wanted to have that person in? Who in the Comptroller's office? Who in the Federal Reserve and who in the Federal Home Loan Bank Board that this subcommittee wants to have another hearing, which I think we do shortly, to find out about policy and things, who do you bring in from each of those places?

Mr. FISHBEIN. Well, I certainly would be glad to share with the subcommittee the names that I know.

Senator DIXON. Let's not do that publicly. Let me simply say that I would ask each of you, particularly those who work with it—and I see Mr. Kolesar nodding that he feels he has some information in that regard—anybody in this room here. I would like to know—we're going to have another hearing on this to find out what they're doing in those separate four shops. Now because there are certain time limitations, I can't have four from each shop. I'd like to have one person from each shop and maybe they could have a couple people with them, that we could ask questions of and so forth and find out some things, and I would ask you to get hold of our staff people here, each of you, and give us several names at the FDIC that you think are key names there on the CRA, at the Comptroller, at the Federal Reserve Board and at the Federal Home Loan Bank Board, and the I think we can do some walking around and figure out who are the people to call.

Mr. BROWN. Mr. Chairman, I have a suggestion. When I was on the Federal Reserve Board's Consumer Advisory Council, they gave us access to CRA examination reports. They would sanitize them like deleting the name of the institution and the name of organizations that provide information, but they gave us the exam report for a number of institutions. Mr. Fishbein got them earlier when he was on the advisory council and there was about a three or four year interval in between the times of those two sets of examinations.

It was very clear that the exams that we got which were later were more comprehensive because you could just see in the evaluation that more serious thought had been given and the analysis was better.

I think one of the things that you could do to best inform yourselves of some of the differences between the agencies is to ask them to provide to the committee a set of CRA examination reports going back for several years, properly sanitized, and allow you to draw some of your own conclusions. If they can provide them to the Consumer Advisory Council, they certainly can provide them to the committee.

Senator DIXON. That's a very good suggestion.

Mr. Kolesar, do you have any suggestions along that line if we're going to have in some representatives from those four agencies about things that we can do to understand better the processes that actually work out there?

Mr. KOLESAR. No, Mr. Chairman, not beyond what Allen and Jonathan have already suggested. I would concur with that and be happy to provide you with some names that we have knowledge of.

Senator DIXON. Mr. Conville.

Mr. CONVILLE. No, Mr. Chairman. We'd be happy to provide names also.

Senator DIXON. Then let me just say to everybody in the room that what we're going to do is see what those four separate regulators have to say about how CRA is functioning there and that all of this has been very, very useful. After we've developed this and so forth, then we will have some meetings among the folks here in the subcommittee and staff and we will probably put together some finalized thoughts at the subcommittee level and then we'll bounce it back off a lot of you people to see how it sounds out there in the country where it would be hopefully important to community groups and financial institutions to make this program work better.

I would have to observe that—and perhaps my colleague wants to make some comments about this—I think you could get all hung up on whether you put a number on this and lose a lot of opportunity to make profoundly good improvements because we would have a division about whether you ought to have some kind of numbers.

I don't think it comes through to me as being so basic you have to put a number on it. But now I'd be interested in hearing more from some of you in the consumer groups that obviously feel more strongly about that. Maybe you want to educate the chairman of the subcommittee a little more about that. I don't get the impression numbers have worked all that well so far anyway.

But anyway, I thank you all for coming today and this meeting is adjourned.

[Whereupon, at 11: 25 a.m., the hearing was adjourned.]

[Responses to written questions and additional material supplied for the record follows:]

QUESTIONS FOR HOWARD B. BROWN FROM SENATOR ALAN J. DIXON JUNE 6, 1989

Q.1. Do you yet have any statistics showing whether Connecticut Public Law 87-24 has had any effect on people's use of depository institutions versus check cashing centers?

1. No statistics are available showing whether Connecticut Public Act 87-24 has had any effect on people's use of depository institutions versus check cashing centers. However, based on a recent survey of licensed check cashers in Connecticut it appears as though PA 87-24 has not had a significant impact on the number of income maintenance check's cashed. Visual evidence and feed-back from the banks point out that the greater availability of banking institutions has reduced the impact in the lobbies of the few institutions which cashed assistance checks before the law was passed.

Q.2. What has been Connecticut banks' experience with check fraud? How much have banks lost from fraud? For how much has Connecticut reimbursed banks? Provide any other data you might have about costs to depository institutions resulting from P.L. 87-24.

2. The Connecticut State Treasurer's Office revealed that of over 7 billion dollars in various categories of check payments made annually, less than $200,000 are lost as a result of fraudulent activity. Following implementation of Connecticut's law, Public Act 87-24, in October 1988, there has been no demonstrable uptick of fraudulent activity. Also, a survey of major Connecticut banks indicated that losses from cashing checks issued by the Connecticut State Department of Income Maintenance and claims for reimbursement were virtually nil.

Q.3. Provide copies of Connecticut Public Law 87-24 and implementing regulations.

3. A copy of PA 87-24 and implementing regulations are enclosed.

Q.4. How has this check cashing law been advertised to government check recipients? If a notice was sent in the mail to welfare check recipients, provide a copy of such notice.

4. A series of public service announcements was issued to members of the broadcast and print media. Notices in English and in Spanish were mailed to all public assistance clients by the Department of Income Maintenance in February and March of this year informing them that public assistance checks could be cashed at any bank in Connecticut. Beginning with August public assistance checks, the Department of Income Maintenance instituted a program of sending reminder notices to clients. The Department of Income Maintenance mails in excess of 100,000 checks per month to eligible public assistance clients amounting to over $29 million in benefits.

Substitute House Bill No. 5558

PUBLIC ACT NO. 87-24

AN ACT CONCERNING THE CASHING OF STATE CHECKS.

Be it enacted by the Senate and House of Representatives in General Assembly convened:

Section 1. (NEW) (a) For the purposes of this section: (1) "Banking institution" means a state bank and trust company, national banking association, industrial bank, state or federally chartered savings bank, state or federally chartered savings and loan association, state or federally chartered credit union or other state or federally chartered banking institution having an office within this state; (2) "recipient of public assistance" means any person receiving public assistance under chapter 302 of the general statutes or the Refugee Program.

(b) Each banking institution shall cash, at its main office or any of its branch offices within the state, any check drawn by the state of Connecticut and payable within the state to a recipient of public assistance, if the check is negotiated to the banking institution by the original payee of the check, and if the payee produces reasonable identification as provided for in regulations adopted pursuant to section 2 of this act. No banking institution shall charge a recipient of public assistance a fee for cashing a check pursuant to this section. Nothing in this section shall preclude a banking institution from requesting a fee from the state of Connecticut for cashing such checks. The provisions of this subsection shall apply to a state or federally chartered credit union only if the original payee negotiating the check is a member of such credit union.

(c) Nothing in this section shall be interpreted as limiting any rights which the banking institution may have against the payee by contract or at law, with regard to items which are negotiated to it as provided for in this section, which are not paid upon presentment or where such payee breaches a warranty made under section 42a-4-207 of the general statutes. This section shall not apply to any check negotiated to a banking institution if such institution has reason to believe that the check will not be paid on presentment or that the tendering party may be in breach of one or more of the warranties contained in said section 42a-4-207.

(d) No banking institution shall be liable to reimburse the state of Connecticut for a loss incurred as the result of the wrongful payment of any check cashed pursuant to this section, provided at the time such check was cashed such banking institution employed the identification procedures prescribed in regulations adopted pursuant to section 2 of this act.

Sec. 2. (NEW) The commissioner of income maintenance, in cooperation with the banking commissioner, shall adopt regulations in accordance with chapter 54 of the general statutes specifying: (a) The forms of reasonable identification which a banking institution shall accept when cashing a check pursuant to section 1 of this act; and (b) the identification procedures such institution shall employ to avoid liability for the wrongful payment of any such check.

Sec. 3. This act shall take effect from its passage, except that section 1 shall take effect October 1, 1987 or on the effective date of the regulations adopted pursuant to the provisions of section 2 of this act, whichever is later.

Certified as correct by

____
Legislative Commissioner.

____
Clerk of the Senate.

____
Clerk of the House.

Approved 4-6-87, 1987

Eff. see Sec 3.
____
Governor, State of Connecticut.

R-80 REV 1-77

IMPORTANT. Read instructions on bottom of Certification Page before completing this form. Failure to comply with instructions may cause disapproval of proposed Regulations.

Page 1 of 3 pages

STATE OF CONNECTICUT
REGULATION
OF

NAME OF AGENCY
Connecticut State Department of Income Maintenance

Concerning

SUBJECT MATTER OF REGULATION
Public Assistance Checks Cashed By Banking Institutions

(NEW) Sec. 17-2-214. Definition As used in section 17-2-215, "banking institution" means a state bank and trust company, national banking association, state or federally chartered savings bank, state or federally chartered savings and loan association, state or federally chartered credit union or other state or federally chartered banking institution having an office within this state.

(NEW) Sec. 17-2-215. Public assistance checks cashed by banking institutions No banking institution shall be liable to reimburse the State of Connecticut for a loss incurred as a result of wrongful payment of any Public Assistance check provided that acceptable forms of identification as described in subsection (a) of this section are used and providing the procedures listed in subsection (b) of this section are followed.

(a) Documents issued by public or private organizations as a means of identifying an individual are considered acceptable forms of identification. The identification document must include the signature of the payee or a unique number by which the organization can identify the payee. Acceptable forms of identification may be issued by the following organizations:

(1) the Department of Income Maintenance
(2) the Department of Motor Vehicles
(3) other state agencies
(4) federal agencies
(5) municipalities
(6) employers
(7) credit card companies
(8) banking institutions
(9) unions

(b) The following procedures will be adhered to when cashing checks:

(1) The check must be signed by the payee at the time of cashing, or signed again if previously signed.

(2) Two acceptable identification documents must be required.

(3) In combination the two acceptable identification documents must present the following:

a) signature

b) photograph

c) a unique number by which the payee can be identified by the organization issuing the identification document

(4) The signature on any identification document must appear to match the signature on the check.

(5) The types of identification documents used must be clearly recorded on the check, or, if recorded on computer or other medium, must include the date of the transaction and be presented to the Department upon notification to the bank of a stop payment action.

(6) An identification number from the identification documents must be clearly recorded on the check or if recorded on computer or other medium, must include the date of the transaction and be presented to the Department upon notification to the bank of a stop payment action.

(7) A clear bank photograph may be substituted for a photo ID.

Statement of Purpose: To adopt a regulation for the Connecticut State Department of Income Maintenance, to comply with the provisions of Public Act No. 87-24.

This month, the Department of Income Maintenance is switching to a new computer system to serve you better. There will be some changes you need to know about. Please read this brochure carefully and save it. Our new computer will improve services for YOU! Please let your worker know if you have any questions or problems!

If you receive an AFDC, State Supplement, or Refugee Assistance Check ...

Starting next month, your check and medical card will come by the 3rd, not on the 1st.

Your check and medical card will look different, too. Your check will be on the left, and your medical card will be on the right. This is the opposite of how they have been attached. Be sure you take the correct part to the bank.

If you pay your rent on the 1st of the month, you may want to tell your landlord that your monthly benefit will be arriving by the 3rd, instead of the 1st.

If you receive State Supplement and have a job, you will have to send a Monthly Report Form to us. The Monthly Report Form will ask questions about your financial situation. You will get more information about this soon.

If you receive State Supplement, your benefit may change very slightly due to a new rounding process. The new computer will round down to the whole dollar when figuring a benefit amount.

Doctors, hospitals, clinics and other health care providers are being told about the new medical cards. If you need medical care between the 1st and the 3rd, your health care provider has a telephone number to call to check if you are covered, or you can call your worker for a replacement medical card.

If You Get Food Stamps...

Next month, your Food Stamp computer card will look different, and it will come by the 3rd, too.

You must sign your Food Stamp card on the back at the bank, just like a check, in order to get your Food Stamps.

Bring your Food Stamp ID card to the bank (and any other form of identification you may have) to assist you in getting your food stamps.

Other Changes...

Your case number will be different.

All notices and forms will look different and will be available in English or Spanish.

You will have one worker assigned to your case and you can call him or her for all of your benefit needs.

AFDC, Medicaid, and Food Stamp redeterminations will be delayed for up to three months while we get our new computer started. You should call your worker to report any changes you have been saving for your redetermination.

ALSO! A new law recently took effect that means you can cash your check at ANY bank as long as you have proper identification. You do not have to have an account at the bank. All banks and their branches must cash your assistance check because of this new law.

FOR RELEASE

STATE OF CONNECTICUT • DEPARTMENT OF BANKING • 44 CAPITOL AVENUE • HARTFORD, CT 06106

December 8, 1988

For more information, contact:
Dave Tedeschi
566-4560, Ext. 8388

Attached is a Public Service Announcement regarding the new regulations for the cashing of state public assistance checks. Please use the information provided at your own discretion.

Should you prefer to tape a PSA with Banking Commissioner Howard Brown doing the audio, please contact me so that we may set up a time convenient to his schedule and yours.

Thank you for assisting the Department of Banking in publicizing this important consumer issue which benefits many of Connecticut's residents.

FOR RELEASE

STATE OF CONNECTICUT • DEPARTMENT OF BANKING • 44 CAPITOL AVENUE • HARTFORD, CT 06106

PUBLIC SERVICE ANNOUNCEMENT

SUBJECT: WELFARE CHECK CASHING REGULATIONS
TIME: 60 SECONDS
DATE: DECEMBER, 1988 JANUARY, 1989

LEAD: HERE IS SOME GOOD NEWS FOR RESIDENTS WHO ARE ON STATE PUBLIC ASSISTANCE.

NEWLY-ADOPTED REGULATIONS NOW REQUIRE ALL CONNECTICUT BANKING INSTITUTIONS TO CASH STATE WELFARE CHECKS AT NO CHARGE FOR ANY PUBLIC ASSISTANCE RECIPIENT WHO ENDORSES THE CHECK AND OFFERS REASONABLE IDENTIFICATION.

WHEN CASHING A CHECK, YOU WILL NEED TO HAVE TWO FORMS OF IDENTIFICATION WHICH TOGETHER SHOW A SIGNATURE, PHOTOGRAPH AND UNIQUE IDENTIFYING NUMBER. ACCEPTABLE FORMS OF IDENTIFICATION INCLUDE A CONNECTICUT DRIVER'S LICENSE, A DEPARTMENT OF INCOME MAINTENANCE PUBLIC ASSISTANCE CARD; A CREDIT CARD; BANK CARD; UNION CARD; OR ANY OTHER VALID ID.

CONNECTICUT IS THE FIRST STATE IN THE COUNTRY TO PASS LEGISLATION THAT REQUIRES ALL BANKS TO CASH PUBLIC ASSISTANCE CHECKS REGARDLESS OF WHETHER OR NOT YOU HAVE AN ACCOUNT. THE CONNECTICUT DEPARTMENT OF BANKING IS PLEASED TO BE PART OF A GOVERNMENT NETWORK THAT IS CONTINUALLY LOOKING OUT FOR THE INTERESTS OF ALL OUR RESIDENTS.

-30-

QUESTIONS FOR WILLIAM E. DOUGLAS FROM SENATOR ALAN J. DIXON
JUNE 6, 1989

Question 1: Your testimony states that the chances of a check being lost, stolen, or seriously delayed are 16 times greater with a paper check than with Direct Deposit. What period of time constitutes "seriously delayed?" The testimony of the American Association of Retired Persons claims that their members have experienced significant delays and lack of access to direct deposited funds when funds are misdirected or a recipient changes bank accounts. What sort of delays are common when funds are misdirected and when a recipient changes accounts? If a Direct Deposit is misrouted or misposted, what percentage are corrected within 2 days? How long do other corrections take? What is the procedure? How can these problems be minimized?

Answer: If Direct Deposit funds are not posted to the proper account and made available to the recipient on the payment date, the recipient contacts the program agency (such as the Social Security Administration) and the program agency forwards a trace action request to its servicing Regional Financial Center (RFC). The RFC verifies payment issuance, confirms the payment was not returned, and sends a computer generated trace action request to the financial institution. All of the above steps are taken within 24 hours of receipt of the agency trace action request. Any followup actions are processed under the same procedure at the request of the program agency.

Approximately 90% of trace actions are resolved as initial items, with 10% requiring followup action. We continue to work on ways to improve our process because our twin goals are as error-free a delivery process and as quick a corrective procedure as is possible.

Given the fact that both account and financial institution routing numbers change when people change banks, when banks and/or Savings and Loans merge, close or restructure, and that--when more than 250 million transactions take place each year--some miscoding errors will occur, we are not certain that a substantial improvement in the 1 in 8,000 ratio can be accomplished. We are currently working on several programs with the financial community in an attempt to minimize these types of errors to the maximum extent possible.

The fact remains, however, that the Direct Deposit ratio is far, far better than the problem check ratio (1 in 500). In addition, the "best case" timeframe for resolving the simplest type of missing check situation--no theft, fraud or forgery is involved--is not short! Several weeks are required to establish the facts and issue a replacement check. If theft, fraud or forgery *is* involved, several months of investigation is the norm.

Question 2: How long does it normally take to set up a Direct Deposit for a check recipient? How much notice must a recipient give in order to change accounts?

Answer: Monthly benefit payments are converted to Direct Deposit in 60-90 days. Because the Social Security Administration (SSA) authorizes such an enormous number of payments, SSA checks are produced by our Regional Finance Centers (RFCs) throughout the month prior to payment date. For example, December payments will be printed beginning in early November. The checks are then enclosed and stored until the U.S. Postal Service delivers them on December 1. Therefore, to convert a December SSA check payment to Direct Deposit, the Direct Deposit signup form must be received by the SSA office in early October. SSA would update its Direct Deposit payment files during October, then deliver payment information to FMS in early November, and the Direct Deposit payment would be posted to the account in December.

Because of the complexities inherent in payment authorization and processing, we doubt if Direct Deposit signups can ever take less than 30 days. In cooperation with FMS, however, SSA has developed a simplified telephone enrollment process which greatly improves the paper process described above. When simplified enrollment is used during the initial application for benefits, the first payment will normally be issued by Direct Deposit. We are also studying a method by which financial institutions could generate automated enrollments for their customers. This process, if it proves viable, will further simplify and shorten the signup process.

Question 3: Do any of your Direct Deposits go to check cashing centers?

Answer: No. Federal Direct Deposit payments may only be sent to financial institutions with established Routing and Transit Numbers.

Question 4: Which recipients like Direct Deposit? Which do not and why not?

Answer: The steady growth in the number of recipients who receive Direct Deposit clearly indicates they appreciate the benefits of Direct Deposit, and, with very rare exceptions, they do not revert back to checks. Current Federal salary participation in Direct Deposit is at 80%; Supplemental Security Income (SSI) payments are at 16.2%. Social Security retirement payments, the largest benefit file by far (over 34 million payments each month), passed the 50% Direct Deposit rate earlier this year and the percentage continues to grow. Although new signups for other Social Security programs continue to grow, enrollment rates for SSI payments have remained relatively low. One reason is that SSI recipients are disproportionately "unbanked." They also suffer from a much higher incidence of lost and stolen checks. Our Electronic Benefit Services test in Baltimore is an attempt to provide them with many of the same benefits experienced by Direct Deposit recipients, even though they may not have a conventional relationship with a financial institution.

Question 5: What is the difference in cost to the Government and to the depository institution of processing a check versus a Direct Deposit payment?

Answer: Issuing a check payment costs the Financial Management Service $.302; a Direct Deposit payment costs $.045. These costs include computer system costs for payment issuance, as well as computer and personnel costs for aftermath processing (such as reconciliation and claims activity for checks and trace actions on Direct Deposit payments). Although we do not have specific information about program agency costs, we believe they are the same cost for check or Direct Deposit payments. Financial institution costs related to check versus Direct Deposit processing vary, and there is no one set of figures available which apply to all financial institutions. Industry estimates, however, indicate that financial institution check processing costs range from $.71 - $1.49 while Direct Deposit processing costs are about $.03 - $.11.

DEPARTMENT OF THE TREASURY
FINANCIAL MANAGEMENT SERVICE
WASHINGTON, D.C. 20227

SEP 28 1989

Dear Mr. Rother:

My staff expresses thanks for the opportunity to meet with Myriam Marquez of your staff, to discuss items to be covered in your upcoming survey about Direct Deposit. We are concerned that questions focused only on Direct Deposit will not provide a complete picture of what Americans think about the Government's major payment mechanisms.

We are quite interested in knowing more about the concerns the public has about payments from the Federal Government. We had hoped to work with you to obtain such information from recipients of Government payments, both those who are paid by check and by Direct Deposit. The findings from a balanced survey would be helpful in identifying possible improvements to both payment methods. Working with your organization can help us obtain the additional information we need to make appropriate decisions about improvements in payment delivery.

We have enclosed several proposed questions which we would like to have answered as part of your survey. If you feel the questions we have enclosed are inappropriate for your survey, please let us know of any changes you would suggest.

We would appreciate your keeping us informed as your survey plans are finalized. We would also be interested in a summary of the survey results when they become available. This information will be the basis for discussions among FMS senior managers regarding our payments management programs.

Sincerely,

Michael D. Serlin
Assistant Commissioner
Field Operations

Mr. John Rother
Director, Legislation, Research
and Public Policy Division
American Association of Retired Persons
1909 K Street, N.W.
Washington, D.C. 20049

Enclosure

PAYMENT MECHANISM SURVEY

GENERAL INSTRUCTIONS:

All respondents are asked to answer the following question:

On a scale of 1 (dislike strongly) to 10 (like strongly), please rate the following:

____Checks ____Direct Deposit ____Money Orders
____Financial Institutions ____Automated Teller Machines
____Check Cashing Services

Answer Part A, if you receive your Federal benefit payment by home-addressed check. Answer Part B, if you receive your payment by Direct Deposit.

PART A - HOME-ADDRESSED CHECK RECIPIENTS

1) Are you aware that Direct Deposit is an option?

If yes, how did you hear about Direct Deposit?
Federal Agency (authorizing payment)___________
Financial Institution____________
Advertising (what kind and where)_____________
Friends and/or relatives___________

2) Have you ever considered signing up for Direct Deposit?
yes____ no____

If no, please
explain____
____

3) Do you read our check messages? yes____ no____

4) Within the last 24 months, have you ever received your check late? yes____ no_____

If yes, How many times?__________
How long did it take to correct the problem?________

5) How much time does it take to cash/deposit your check?

6) Have you ever experienced difficulty cashing your check?

7) Do you know who to contact if there is a problem receiving your check?

8) Have you ever received your payment by Direct Deposit?

9) How would you improve the way the Government makes benefit payments?

PART B - DIRECT DEPOSIT RECIPIENTS

1) How long have you used Direct Deposit?_____________

2) What are your reasons for using Direct Deposit?

3) How did you hear about Direct Deposit?
Federal Agency (authorizing payment)_______
Financial Institution_______
Advertising (what kind and where)_____________
Friends and/or relatives__________

4) Within the last 24 months, has your Direct Deposit payment ever been late? yes____ no____

How many times?__________
How long did it take to correct the problem?___________

5) Within the last 24 months, has your Financial Institution denied access to your funds on the scheduled payment date? yes____ no_____

If yes, How many times?______
How long did it take to correct the problem?______________

6) Do you know who to contact if there is a problem receiving your Direct Deposit payment? yes_______ no_______

7) How would you improve the way the Government makes benefit payments?

DEPARTMENT OF THE TREASURY
FINANCIAL MANAGEMENT SERVICE
WASHINGTON, D.C. 20227

COMMISSIONER

October 16, 1989

Dear Mr. Chairman:

Per your request of September 18, 1989, I am pleased to furnish further information to supplement my June 6th testimony.

In my testimony I stated that the chances of a payment being lost, stolen or significantly delayed are 15 times greater if it is made by check than by Direct Deposit. The facts are: In Fiscal Year 1988, 546,600,000 check payments were issued, and 1,068,133 initial complaints of non-receipt were received on these payments. Therefore, one of every 512 check payments resulted in a preliminary inquiry concerning non-receipt. For the same period, 287,900,000 Direct Deposit payments were issued, and 34,752 initial complaints of non-receipt were received on these payments. Therefore, one out of every 8,284 Direct Deposit payments resulted in a preliminary inquiry concerning non-receipt. Timely production and delivery of Government payments is one of the most critical functions of this organization; consequently, we label as "significantly delayed" any payment, check or Direct Deposit, if it is not received on the payment due date.

Following the Committee Hearings, Michael Serlin, the Financial Management Service's senior executive responsible for all of our payment programs, met with John Rother, American Association of Retired Persons' (AARP) Director of Legislation, Research and Public Policy, to learn more about their concerns. It appears that AARP's reservations about Electronic Funds Transfers are based on some responses received from an item printed in its November 1987 newsletter. The item encouraged payment recipients to share any problems they had encountered with Direct Deposit payments. Although we were not told specifically how many responses were received, the number, apparently, was rather small in both absolute and relative terms. Because each one of the 250 million EFT payments in 1987 had the potential to go astray, the universe of possible complaints was huge. Even more important, however, was the fact that the newsletter did not solicit reader feedback about check receipt problems during a comparable timeframe. Because of that defect, we cannot draw any valid or useful conclusions from the material.

In order to gather data from which conclusions can be drawn about product quality, we have offered to work closely with AARP and attempt to measure the public's reaction to both the check and Direct Deposit payment systems. I have enclosed a copy of Assistant Commissioner Serlin's recent letter to AARP containing the survey questions we have proposed. No matter the outcome of the survey, we hope the information gained can be used to make improvements in both systems. In addition, we offered to work with AARP in developing various consumer-interest type material to further educate the public about key aspects of the two payment programs and we are hopeful that these efforts will also bear fruit. During our meeting, Mr. Rother made it clear that AARP does support Direct Deposit; their main concern is the possibility that Direct Deposit might be made mandatory. We advised them that we do not advocate mandatory Direct Deposit for Social Security and other benefit payments. We know Direct Deposit has an impressive track record of on-time delivery of funds in a safe and convenient manner, and at a much lower cost than checks. Our marketing strategies are built on the premise that the product sells itself if people are informed about its advantages over checks.

We have used the enclosed Question and Answer format to address the other questions you have raised. I hope that our information will assist your Committee in its effort to provide the best possible benefits to our citizens. Thank you for the opportunity to be a part of that effort.

Sincerely,

W.E. Douglas

W.E. Douglas

The Honorable Alan J. Dixon
Chairman
Subcommittee on Consumer and
  Regulatory Affairs
Committee on Banking, Housing
  and Urban Affairs
United States Senate
Washington, D.C. 20510

Enclosure

NaCCA
National Check Cashers Association, Inc.

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ADMINISTRATIVE OFFICES:
1135 Clifton Avenue
P.O. Box 2666, Clifton, New Jersey 07015-2666
201-777-9870

November 6, 1989

Senator Alan J. Dixon
Chairman, Subcommittee on Consumer
and Regulatory Affairs
Washington, D.C. 20510-6075

Dear Senator Dixon:

This letter is in response to the questions asked in your letter dated September 18, 1989.

QUESTION 1. Page one of your testimony claims that the great majority of professional check cashers provide reasonably priced services. What are reasonable prices for cashing a government check, writing a money order, and electronically paying bills?

ANSWER 1. A reasonable price for check cashing services must necessarily vary from place to place. This is because, in those states where check cashing fees are unregulated, the fees in each region or neighborhood are determined by a number of market factors including the usual costs of doing business, the location of the store (inner city vs. suburb), the risk factors, the numbers of transactions handled, population density in the vicinity of the store, pricing policies of local competitors such as banks, supermarkets and other check cashers, the method used to distribute government benefits, the percentage of customers receiving government benefits, the products and services available (check cashing, money orders, money transfers, transit fares, etc.), the mix of the transactions handled, etc.

In regulated states, the regulatory agency responsible for establishing rates takes into account most of these same factors.

Furthermore, in a recent decision rendered in a case in the United States District Court in the State of Connecticut, the Court held that a check casher is entitled to a fair and reasonable return for its services as a matter of law, and that local market factors must be considered when establishing a rate, i.e., that a rate in one jurisdiction does not automatically justify the rate in another jurisdiction.

It is therefore not possible to specify a uniform nationwide price for cashing a check or selling a money order because of the wide range of regional variations that have a material effect on the fees charged by a given check casher.

However, we believe that the range in fees to cash a government benefit check is 1% to 3%, keeping in mind that a fee that is reasonable in one place may not be reasonable in another place. Rates must necessarily be considered along with any additional services provided free or below market prices, such as money orders, as well as the other services provided such as utility bill payments. As stated above, the range differential of 1% to 3% is determined by the market factors we discussed above, including the location of the store (inner city vs. suburb), the risk factors, the number of transactions handled, the average size of the transactions handled, population density in the vicinity of the store, pricing policies of local competitors such as banks, supermarkets and other check cashers, the method used to distribute government benefits, the percentage of customers receiving government benefits, the mix of the types of transactions handled, the products and services available, etc.

But it should be understood that the wide variety of government checks includes not only benefit checks such as Social Security and SSI benefits, welfare benefits, veteran's benefits, and unemployment compensation but also municipal, county, state and federal payrolls and tax refunds. The rate charged for these types of government checks varies according to risk, recognizing that the risk involved in cashing Federal checks is higher because they are delivered through the mails and because of the slow and cumbersome Federal reclamation procedures. For example, tax refunds are particularly troublesome to the check casher since they are delivered once a year through the mail and are cashed for customers who may not be regular customers. These people may not cash a check at a bank, because they lack sufficient balances to cover the amount of the check.

Money orders fees range from nothing to $1.50, with most fees falling below $1.00; banks charge from $2.00 to $3.50. These rates are important to consider when comparing the cost of financial services provided by check cashers and banks.

There are several reasons why the fees charged by check cashers should not be considered in a vacuum. In addition to check cashers and traditional banking institutions, there is no shortage of options and alternatives available to convert a check into cash, e.g., grocery stores, liquor stores, neighborhood businesses, friends and relatives. And the price that a person pays to cash a check or purchase a money order is a function of the convenience and level of service desired. Someone who is willing to put up with long lines and inconvenient hours of operation may pay less than someone who requires quick service and more convenient hours of operation.

Dealing with a check casher may be more or less expensive than the other available choices since it depends upon the needs and desires of the consumer, the area of the country, state or municipality in which you are located, the level of service required and the type and complexity of the transactions the consumer performs every month.

Regarding bills paid electronically, the consumer is normally not charged a fee, since a fee is generally paid to the check casher by the company whose bills are being collected.

QUESTION 2. Provide copies of the codes of conduct you provide your members, which is referred to on page one of your testimony.

ANSWER 2. The attached Statement of Policy is the code of conduct we provide to our members.

QUESTION 3. What would a welfare recipient have to pay on average to cash a $500 benefit check? What are the range of prices charges by check cashing centers? What on average would it cost a check cashing center to cash such a check? Explain how you calculated these costs and provide what the range of costs might be for different check cashers.

ANSWER 3. As we explained in our answer to Question 1, a welfare recipient could pay anywhere from nothing (in a place like New York City where welfare benefits are delivered electronically and the City pays the fee) or from 1% to 3% to cash a $500.00 benefit check. The price depends to a large extent upon the cost of doing business where the customer is located and the level of service and convenience the customer demands.

The cost to cash a check depends upon several variable business factors including the normal retail business operating expenses such as rent, insurance, utilities, payroll, cash delivery and bank service charges. In addition, the check casher has some special cost factors to consider, such as a more sophisticated security system, higher than normal theft insurance premiums, bad check losses, and special bonding requirements applicable to our industry as primary distributor of food stamps. The number and type of free services included with cashing a check must also be taken into account.

As with all retail businesses, the various cost elements are highly variable and depend on the marketplace in which a check casher operates. Therefore there is not single uniform cost to cash a check.

Other vital variables include 1) the monthly transaction volume-the cost per transaction in a location cashing 5,000 checks per month would obviously be less than one cashing 2,500 checks per month; 2) the mix of services offered - from a cost accounting standpoint, the mix of services exerts a tremendous influence on the cost per item handled, considering the kind of checks cashed and the amount of income from other services; 3) other services offered - if a location offers check cashing as a supplement to its main business, the cost of cashing a check could be less, but the service level would be lower because the owner would no doubt concentrate on the products and services where most of the revenue is derived; 4) the location of the store - inner city sites have higher occupancy costs when compared to suburban locations; and 5) quality of service - the level of service demanded by and therefore offered to the consumer will have an impact on the cost per transaction.

Customers are free to choose the level of service they want and they should continue to have a wide choice of establishments to patronize for their financial transactions.

QUESTION 4. What is the typical range that a person would spend per month at a check cashing center? How would this amount compare to the typical range of fees a person would spend on a no-minimum-balance bank account.

ANSWER 4. The amount that a typical customer would spend per month at a check cashing center is not possible to project, because of the factors cited in our answers to Questions 1 and 3. In addition, one has to consider the number and kind of transactions needed, such as cashing checks, purchasing money orders, initiating money transfers, etc. It should also be pointed out that what may be the best way for one person to handle personal financial affairs may not be acceptable for another, taking into account economics, convenience and the element of personal choice. For example, most people find it convenient to maintain a checking account and use credit cards; others prefer to deal in cash and avoid the problems associated with reconciling bank accounts, bank service charges, return item charges that range from $10 to $30, and expensive credit card annual fees and interest charges.

We have provided some examples showing the cost of purchasing a typical mix of financial services in different areas of the country and even the variations that occur within the same area. One operation may charge a slightly higher fee to cash a check but offer free money orders and later hours; another in the same area may charge less for check cashing but charge higher fees for money orders and other services. This affords consumers the choice to deal with the business that best fits their individual needs. Some examples follow:

CALIFORNIA

Business	Cost to Cash a $500 Check	Cost for 5 Money Orders	Total
Check Casher A	$9.50	Free	$ 9.50
Check Casher B	$7.50	$ 1.25	$ 8.75
Bank of America (savings account customer)	$1.00 (mo. fee)	$12.50	$13.50
Bank of America (non-customer)	$5.00	$17.50	$22.50

ILLINOIS

Check cashing fees are regulated to be no more than 1.2% + $0.90 per item, the maximum money order fee is 1% + $0.75.

Business	Cost to Cash a $500 Check	Cost for 5 Money Orders	Total
Currency Exchanges (Check Cashers)	$6.90	$ 2.50 - $6.00	$ 9.40-$12.90
First of Chicago	$0.00	$10.00	$10.00

COLORADO

Business	Cost to Cash a $500 Check	Cost for 5 Money Orders	Total
Check Casher A	$8.00	$ 0.95 (if $100 or less)	$ 8.95
Check Casher B	$7.50	$ 0.00	$ 7.50
Colorado Natl Bank	$2.00	$12.50	$14.50

Senator Dixon
Page six

We recognize that a consumer can maintain a checking account and pay bills for less cost than the examples above, but this is not relevant to those patrons who choose the ease and simplicity of dealing primarily in cash, and who prefer the convenient hours, convenient locations and the services offered by check cashers. The option of low cost checking is still available for those who make that choice. In addition, there are many people who maintain checking accounts who use check cashers for convenience and in those instances when they have a check that is larger than the balance in their account. In general, banks don't cash checks - they advance money against funds on deposit so you must have funds in order to cash a check. Check cashers advance their own funds when they cash a check. We believe that it is neither necessary nor desirable to force consumers to establish and maintain checking accounts.

QUESTION 5. How many check cashing locations are there in the United States? How many does the National Check Cashers Association represent?

ANSWER 5. Although there are no definitive survey data available, we estimate that there are between 3,000 and 5,000 check cashing locations in the United States. The current membership of NaCCA is 600 companies, with 1,500 locations operating in 24 states.

I hope the answers provided herein will be of assistance to the Subcommittee in its consideration of S.906, the Government Check Cashing Act of 1989. Please let us know if we can be of further assistance.

Very truly yours,

Jerome Gagerman (la)

Jerome Gagerman
Chairman
National Check Cashers Association, Inc.

NATIONAL CHECK CASHERS ASSOCIATION

STATEMENT OF POLICY

The professional check cashers of the United States form a well-established and growing alternative to traditional banks for a large and growing segment of the American public. The proprietors of these small businesses operate in a responsible and efficient manner so as to make available to that segment of the public which does not have convenient access to traditional banking channels an outlet through which currency is made available to provide for basic human needs such as the purchase of vital goods and services.

Check cashing facilities have become increasingly important delivery points for financial services as banks have raised their fees and minimum balance requirements and closed large numbers of urban branches for economic reasons.

Professional check cashers are dedicated to operating convenient neighborhood facilities to cash checks and offer a wide variety of ancillary financial services to the public. In addition to cashing checks, these facilities issue money orders, arrange electronic money transfers, accept utility payments, provide credit card cash advances and offer notary public services.

They are utilized by state and municipal governments as conduits for the distribution of welfare benefits and food stamps, for the sale and distribution of automobile license plates and title transfers, and for the sale of transit fare tokens.

In recognition of the vital role played by professional check cashers in the financial services industry, the National Check Cashers Association, on behalf of its members - the professional check cashers of the United States - advocates the provision of these vital services at a fair and reasonable cost to the consumer. The National Check Cashers Association deplores the charging of exorbitant and unfair fees by unscrupulous fringe operators.

In furtherance of these principles the National Check Cashers Association has established the following set of guidelines with which all of its members have voluntarily agreed to comply:

1. Fees charged to consumers should be fair, reasonable and not excessive.
2. Fees should be posted prominently and in full view of the consumer.

3. Customers should not be obligated to purchase any other products or services in conjunction with the cashing of a check.

4. Identification procedures should be reasonable and prudent so as to provide protection against loss to the check casher without entailing undue invasion of the customer's right to privacy.

5. Products and services should be available to all customers on a non-discriminatory basis.

RESPONSES OF ROBERT L.STEVENS
FROM SENATOR ALAN DIXON
REGARDING LEGISLATION ON BASIC BANKING
AND MANDATED GOVERNMENT CHECK CASHING

QUESTION 1. What definition of basic bank account is used in the American Bankers Association annual surveys? Is this definition any more specific than the description included on page 15 of your testimony, "an account that offers limited banking services to the general public at no cost or reduced cost?" The Consumer Federation of America claims in its testimony that a $200 required minimum balance account would still fit your definition of a basic bank account. Is this the case? Do free checking accounts offered only to senior citizens or students qualify as "basic bank account?"

ANSWER 1. The survey describes a basic bank account as an account which offers "limited banking services to the general public at no cost or reduced cost. Typically, minimum balance requirement for these plans are low or non-existent, and debt transactions and/or the number of checks written are completely free or free up to a minimum."

While a $200 minimum balance requirement does not disqualify an account as a basic bank under the definition of our survey, many banks impose no minimum balance requirement. For instance, only four percent of the largest bank (over one billion dollars in assets) offering basic bank accounts impose any minimum balance requirement (73 percent of the largest banks offer basic bank accounts). Only 9.1 percent of banks with assets between one half billion and one billion dollars and only 15.4 percent of banks with assets between $50 and $100 million impose a minimum balance requirement.

According to our 1988 survey, 61 percent of banks offer or plan to offer basic bank account to the general public. This figure excludes accounts offered only to students or senior citizens. A separate question in the surveys addresses the availability of those special accounts.

QUESTION 2. What is the typical range of fees on a no minimum balance banking account? What is the typical range that a person would spend per month at a check cashing center?

ANSWER 2. The median charge on an account without a minimum balance requirement is $2.00 ($2.62 for banks with assets under fifty million dollars).

We do not have any data on the typical range of fees a person would spend per month at a check cashing center.

QUESTION 3. If, as your testimony argues, cheaper services are already available at banks than at check cashing centers, why do so many people use the significantly higher priced centers?

ANSWER 3. As we have noted in our testimony, there are many broader social reasons why some individuals shun banks in favor of check cashing facilities. Many of these reasons are not related to the cost of a bank account or to any reluctance of banks to cash government checks for noncustomers. Indeed, this was illustrated by the May, 1989 testimony of Howard Brown, Banking Commissioner of the State of Connecticut before the Senate Banking Subcommittee on Consumer Affairs on the effectiveness of Connecticut's law requiring banks to cash government checks for noncustomers (Connecticut indemnifies its banks against fraud losses under this statute). In response to the question of whether more Connecticut citizens were now using financial institutions to cash their government checks, Mr. Brown answered, "No." He continued, "The same number of people are going to more banks." Similarly, the Consumer Federation of America ("CFA") concluded in its September 1987 "National Survey Check Cashing Outlets" that consumers would generally pay less at banking institutions than at check cashing centers and would get more for their money. Yet many still fail to use banks. Other studies agree that those without bank accounts seldom cite high service charges or minimum balance requirements as the reasons they lack an account. In fact, the study by Brittain Associates, Inc. conducted with the cooperation of the Atlanta Community Reinvestment Alliance and the First Trust Company Bank of Atlanta, reported that 70 percent of respondents without checking accounts would not open one even if it were offered at no charge.

Some reasons given by these individuals for using non-bank alternatives include:

- comfort with their present personal cash management system and possible unacceptability of personal checks;
- perceived simplicity of the check cashing and money order system compared to bank account;
- fear of overdrafts;
- desire for close, personal control over money and/or lack of familiarity with banks;
- inconvenience of bank location or business hours;
- illiteracy and innumeracy;

- lack of minimal fluency of English;
- belief that they have insufficient funds and/or transactions to justify having an account.

NOTE: Above information referenced from the following:

"Basic Banking," Federal Reserve Bulletin, April, 1987, pp. 262-265.

"Low-Icome Banking Needs and Services," Journal of Retail Banking, Fall 1988, pp. 33-37.

"Survey of Low-Income Households Without Checking Accounts," Unidex Corporation; March 1985.

"All Deserve Access to Services Say Most But Don't Make It a Law, American Banker's Consumer Survey, 1989, pp 22-24.

QUESTION 4. Check cashing centers apparently are growing rapidly in many parts of the country. Are they taking away the banking industry's customers? Does it trouble the banking industry that it is losing 12 to 21 percent of its potential market?

ANSWER 4. ABA encourages it members to offer basic bank accounts and to make individuals without accounts aware of the availability of these accounts. Many banks have successfully marketed such accounts, although promotion could be improved so that more people without accounts will take advantage of the accounts.

QUESTION 5. The National Bankers Association testified that 75 to 90 percent of consumer accounts in most minority financial institutions have an account balance of less than $1000. Do you have any corresponding data for the banks you represent? In what percentage of checking accounts do customers write 10 or fewer checks per month?

ANSWER 5. The average daily account balance for regular checking accounts and for basic bank accounts according to our 1988 survey varies as follows:

	Asset Size (In Million Dollars)				
	Less than 50	50-100	100-500	500-1,000	1,000 or more
Regular Account	$ 942	$1,854	$1,510	$1,584	$1,597
Basic Account	$ 478	$ 538	$ 430	$ 419	$ 400

We do not have figures showing the percentage of checking accounts on which fewer than 10 checks per month are written.

QUESTION 6. The Independent Bankers Association of America proposed that a better way to reach America's underbanked population is to link the cashing of government checks with some type of bank account. What do you believe are the best ways to reach the underbanked--whether they are 12 or 21 percent of American families? Should everyone have a checking account?

ANSWER 6. One of the obstacles to maintaining a bank account appears to be lack of awareness that check services are available from local depository institutions at low cost. ABA can encourage banks to communicate this availability.

A second way to reach those without accounts is through the development of electronic benefits services ("EBS"). EBS offers tremendous promise and opportunity in terms of introducing depository institutions and new technology to those without bank accounts. EBS deliveries government benefits electronically to recipients without bank accounts; recipients then access benefits at a variety of sources through the use of special cards. These programs offer safe and immediate access to funds, encourage checking relationships, and provide recipients with the most up-to-date banking services and technologies.

Rather than relegating recipients to an outmoded and cumbersome payment system, under EBS programs, recipients are helped to use new technologies. Familiarity with electronic systems conveys a sense of integration with the mainstream of society and builds self esteem and confidence. Moreover, the exposure to EBS may encourage individuals to develop account relationships as they become comfortable with banking technologies and systems.

Thus far, evaluations of EBS programs show a high level of satisfaction among benefits recipients. Results have shattered assumptions that the elderly, lower income, and less educated people are unwilling or unable to use electronic payment systems. The projected potential benefits are being realized. The target groups of many of these programs are those individuals who lack bank accounts.

With regard to the question of whether everyone should have a checking account, ABA finds itself in the mainstream of views in that we endorse this goal, but we do not believe that a federal mandate is the best way to achieve it. A Trans Data Corp. public opinion survey administered in March and April found that while many respondents agreed with the concept of basic bank accounts, a significant majority, 69 percent, answered that the government should not mandate such an account. An American Banker article detailing this survey is attached. (American Banker is an independent trade publication not affiliated with ABA). Thus respondents distinguish between the goal of having basic accounts available to all who want them and a mandate requiring that they be available from each and every bank.

Furthermore, as we enumerated in our testimony and question 3 above, there are many reasons other than lack of availability or cost that individuals do not have accounts. One reason is that some individuals are simply uncomfortable dealing with banks, a feeling often compounded by illiteracy or a lack of fluency in English. Still other individuals are concerned that they may overdraw their checking accounts, resulting in penalty fees. In sum, habit, lack of information, and educational and sociological barriers play a far larger role than the availability of such services from banks or their pricing.

ABA believes every American should be able to have an affordable checking or savings account if they wish. Eighty-eight percent already do. One hundred percent probably never will due to a combination of individual and sociological factors. To increase the percentage of bank account holders, the government needs to do a better job of conveying to low-income individuals the benefits of establishing an account relationship, and the banking industry needs to do a better job of communicating the wide availability of affordable basic banking accounts. We believe that through cooperative efforts and without legislative mandates we can achieve a situation in which everyone who wants a bank account has that bank account.

QUESTION 7. The Federal Financial Institutions Council issued a joint policy statement encouraging depository institutions to offer basic banking services and asking trade associations to monitor compliance. How are you monitoring compliance? According to the General Accounting Office only 18 percent of banks and thrifts offer a "lifeline" type account to the general public. Why are only 18 percent complying?

ANSWER 7. ABA has been monitoring the availability of basic bank accounts since 1986 through annual surveys. Our 1986 survey showed that 47 percent of banks offered basic bank accounts; our latest survey reflecting 1988 data showed an increase to 53 percent, with an additional 8 percent planning to offer them.

With regard to the question on the GAO study, we must note that the GAO survey was conducted in August 1985. The joint policy statement by the Federal Financial Institutions Examination Council encouraging financial institutions to offer basic bank accounts was not issued until October, 1986. In 1985, when GAO conducted the survey, the concept of basic banking was relatively new. ABA had just mailed to every member bank a "Voluntary Effort" kit which encouraged basic banking and offered advice on designing a basic bank account. Since the GAO survey, banking regulators and the banking industry have promoted basic bank services and indeed the percentage of banks offering such services has steadily risen.

QUESTION 8. What provisions would be necessary to add to S. 907 to adequately protect depository institutions against fraud?

ANSWER 8. One of the most disturbing aspects of mandating basic bank accounts without allowing depository institutions the discretion to deny or close accounts is the inevitable fraud which could accompany mandatory availability. Moreover, such accounts could serve as useful tools for drug traffickers if banks lack sufficiently broad discretion to close or deny them.

Under S. 907, virtually anyone may insist on an account regardless of their financial or criminal history. The attached article published in the August 3, 1989, issue of American Banker illustrates vividly the potential damage. The article reports the estimated $15 million lost through a check cashing scheme. According to the report, criminals used stolen identifications to establish accounts and obtain credit cards. A detective handling the case relayed that one suspect confessed that the group cashed checks worth $5 million last year, drawn on about 20 different banks. The article reports, "But officials don't yet have a finger on the exact magnitude or cost of the crime as a new evidence, names, and complaints turn up constantly." Seized in the investigation was a "How to Defraud Banks and Vendors" manual, prepared by alleged criminals which lists ten banks identified as "easy targets" for fraud. The manual recommends obtaining various drivers licenses in order to open fraudulent accounts.

The case is one scam which was actually investigated and detected. However, other scams continue and flourish, in part because law enforcements agencies are hard pressed to devote scarce and valuable resources to economic crimes, particularly today when drug and violent crimes have become so prevalent and consuming. As one detective stated, "In the retail and law enforcement community, there's not a lot of manpower devoted to economic crime. There is no way manpower can be devoted to fight this problem." For these reasons, the burden of fraud prevention rests even more on the banks.

Mandating that the banks indiscriminately open accounts for virtually all applicants presents a golden opportunity for criminals, particularly in light of the recent funds availability law. That law requires institutions to release funds before they know them to be collectable. Multiple accounts and unfettered access to funds present an attractive combination to organized crime. For instance, a person could insist on opening an account and after 30 days, deposit a fraudulent certified or cashier's check of $50,000 or even more. Under the funds availability statute, the individual may demand to withdraw that amount of money on the day after deposit, long before the bank may learn of the check's uncollectibility.

One way to protect depository institutions from the losses from fraudulent use of mandated accounts is through government indemnification against losses. Otherwise, any legislation must, at a minimum, allow banks broad discretion in deciding to whom they should open accounts and with whom they should maintain them. Equally, such a standard must not obligate banks to open accounts to known or suspected drug dealers or disclose explicitly the reasons for closure or denial.

It is be extremely difficult, however, to translate a standard for reasonable denial into statutory language without being too vague or too rigid. For example, the "reasonable cause to believe the check is uncollectible" standard contained in the Expedited Funds Availability Act is so strict that it is unusable as a practical matter.

Any legislation mandating that banks offer basic accounts should allow banks to deny an applicant or close a current account if the bank has adverse information indicating that the consumer is unable to manage an account or that the account may beused for fraudulent or criminal purposes. Banks should be allowed to rely on the consumer's financial and criminal history. Furthermore, banks should be permitted to deny an account if it is unable to verify or obtain basic information such as the customer's residential address or financial history.

QUESTION 9. The testimony of the Connecticut Banking Commissioner and the Consumer Federation of America both state that fraud can be virtually eliminated by training tellers to compare signatures on the check and identification card and a signature card on file. Do you disagree with their testimony?

ANSWER 9. Yes, we disagree that fraud maybe virtually eliminated by training tellers to compare signatures of the check, identification card, and signature card on file. As the attached article illustrates, false identifications are easily obtained. The article reports, "To indicate the scope of the scam, Mr. Williams noted that two of the people under arrest used eight different names to open checking and credit accounts under false pretenses."

False identification cards are easily fabricated. Thus, verifying signatures will not prevent many types of fraud.

QUESTION 10. Page 12 of your testimony states that there is no way for a depository institution to ascertain whether an applicant for government check cashing services already maintains a relationship with another depository institution. Why is there "no way?"

ANSWER 10. Banks do not report to any central file the name and other information of their account holders. Such information is naturally highly confidential. In fact, for many banks without the new highly sophisticated centralized systems, the information is not necessarily available among branches of the same bank. Thus, unless a bank wishes to contact every bank and every bank agrees to disclose to any caller private information of its customers, there is no way to ascertain or verify whether an applicant maintains other banking relationships. As we stated in our testimony, legitimate customers will undoubtedly answer honestly whether they maintain a banking relationship elsewhere. Banks cannot, however, be sure of the veracity of statements from individuals intending to commit check fraud. And of course, such individuals may open accounts at different banks,or at different branches of the same bank, using different names and identifications.

All Deserve Access to Services, Say Most, But Don't Make It Law

Consumers apparently fear that a government mandate on lifeline accounts will lead to higher costs for everyone.

BY JAY ROSENSTEIN

The majority of Americans believe banking services are an entitlement – that they should be available to everyone regardless of ability to pay.

But according to the *American Banker* consumer survey, two-thirds of the people do not want the government to require banks to provide basic packages of banking services, known as lifeline accounts, to the poor.

Nor does the public favor laws that require banks to make loans in their local areas, even if the institutions will lose money. This suggests that consumers would prefer governments to refrain from rules that specifically prohibit the discriminatory lending practices commonly called redlining.

These attitudes – liberal on the aspect of entitlement but opposed to government intervention – are found in the sixth annual consumer survey conducted for *American Banker* by Trans Data Corp., its research affiliate in Wayne, Pa.

The results, from interviews of 1,009 randomly selected subjects in March and April, suggest that while Americans have charitable hearts, they fear that if banks are forced to provide services in unprofitable markets, those costs will be translated into higher fees or reduced services for the general population.

The concept of lifeline accounts is a politically, economically, and racially divisive issue that seems to resurface periodically. On the assumption that fees and balance requirements make it difficult for low-income consumers to maintain bank accounts for basic needs like paying the rent, some members of Congress are likely to push in coming months for legislation that would mandate lifeline accounts.

Points to be debated are how a barebones but useful account could or should be structured – such as limiting checks per month and eligibility by income – and how much it will cost financial institutions or taxpayers.

Split Decisions

Attitudes toward a lifeline banking requirement.

[illegible]	[illegible]	[illegible]	[illegible]
Over $50,000	[illegible]	[illegible]	[illegible]
Age			
18-39	[illegible]	64%	9%
40-64	26%	67%	7%
Over 65	16%	78%	7%

Source: American Banker Consumer Survey [illegible]

Don't Bother Us

If the *American Banker* survey is any indication, most citizens would prefer that the issue go away. The responses on this subject, coming almost entirely from people who are users of banks and other depository institutions, were as follows:

- 57% agreed that everyone is entitled to basic banking services, such as a low-cost checking or savings account,

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Jay Rosenstein is an American Banker reporter in Washington.

even if they cannot pay the going price. About 35% disagreed and 9% were unsure.

- 25% said the government should require free or low-cost banking services "even if the bank loses money doing so." But a strong majority – 69% – disagreed. About 6% said they are not sure.
- 25% said banks should be "required to lend locally, even if such loans aren't profitable." But 67% opposed laws mandating where loans are made and 8% gave an unclear response.

On the subject of lifeline accounts, fewer people favor legislation than in an *American Banker* poll five years ago, when 58% said the government should require affordable accounts for low-income people and the elderly poor. At the time, 37% said the government should subsidize the costs of serving the indigent, while 30% said the banks should provide the subsidy.

Because the 1984 and 1989 survey questions were phrased differently, exact comparisons are difficult, but the drift appears to be conservative.

Racial and Income Splits

The groups that most opposed government intervention were the elderly and people with high incomes. Of those over 55 years old, 79% opposed lifeline requirements and 78% opposed redlining restrictions. Of those with $50,000 or more in annual household income, 76% opposed basic banking statutes and 71% opposed laws against redlining.

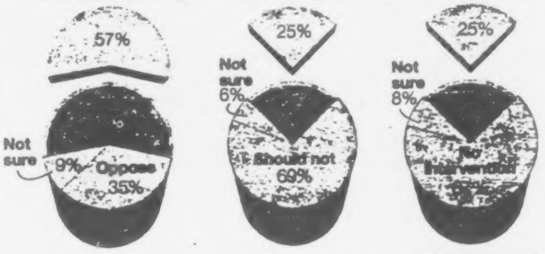
Nonwhites were more inclined to want the government involved. Among nonwhites, 69% saw basic banking as an entitlement (versus 55% of whites), 36% favored laws requiring it (compared with 24% of whites), and 31% said banks should be required to offer the accounts (as did only 24% of whites).

Lifeline and Redlining: An Unclear Mandate

A majority of consumers say everyone is entitled to low-cost, basic banking services . . .

But only one-fourth say the government should mandate it . . .

And one-fourth say the government should force banks to lend in local areas.



Percentages rounded

Source: American Banker Consumer Survey 1989

Also more liberal than average on these issues were young adults. Of people 18 to 39 years old, 31% wanted a lifeline requirement and 33% favored antiredlining laws.

Segmenting the population of young adults a little differently, 35% of those 18 to 34 and earning less than $50,000 a year endorsed the lifeline concept and 38% liked the idea of antiredlining regulations.

The majority's suspicion of government intervention may be a legacy of the Reagan years.

"People realize there's no free lunch," said Allan Paro, director of advertising for the American Bankers Association. "Most of the people realize somebody is going to have to pay for [subsidized or unprofitable services], and they envision they're going to have to bear the cost through higher fees, interest rates, or whatever," he said.

Mr. Paro, who is responsible for most of the market research for the Washington-based trade group, said the *American Banker* survey closely tracks what he has seen in recent ABA focus groups and other consumer studies.

Neil J. Fogarty, president of the Consumers League of New Jersey, Montclair, said the *American Banker* findings may underestimate the number of consumers who would support a requirement that banks offer no-frills accounts. His reason: The phrasing of the question implied that these accounts are likely to be money losers for the bank, which may have colored consumers' responses.

"The big assumption that banks lose money is unwarranted," he said. "The industry alleges it loses money on small accounts, but they lose a lot more on loans to Brazil. I don't necessarily accept the fact that operating a traditional, retail consumer bank with lots of lit-

> "The industry is getting taxpayers to finance a multibillion-dollar bailout of the thrift institutions. So we will not accept the idea that banks are losing money on these small accounts."
>
> *Neil J. Fogarty*
> *President, Consumers League of New Jersey*

VOICE OF THE CONSUMER

> "If you don't have $50 you can't open a savings account. America is supposed to be the land of opportunity. Everyone is not getting those [illegible] opportunities."
>
> *Sixty-seven-year old, married white male living in a rural area*

tle accounts and with low-cost services would necessarily lose money."

Mr. Fogarty cited the example of the $1.5 billion-asset Amalgamated Bank of New York, which is thriving on low-cost checking accounts and consumer loans for working-class customers. Amalgamated, which is owned by the Amalgamated Clothing and Textile Workers Union, touts its affinity to labor and its support for lifeline banking in advertisements.

Mr. Fogarty also said that basic banking services are a logical extension of the "unique social obligations" of banks.

Call for a Compromise

"They safeguard our money. They lend out our deposits. The federal government insures our deposits. The local economy depends on the banks making loans and mortgages," the consumer advocate said. "And now the industry is getting taxpayers to finance a multi-billion-dollar bailout of the thrift institutions. So we will not accept the idea that banks are losing money on these small accounts."

Most bankers contend that almost any no-cost or low-cost account designed by the government and not by private enterprise will end up having to be subsidized in some form, either by the institution or the government – meaning the tax-paying and banking public.

"I don't have any beef with the issue as a public policy issue, but don't design the product for me," said John M. Kolesar, former president of the $40 million-asset Ameritrust Development Bank, Cleveland, which specializes in financial services to low- and moderate-income citizens. He calls for "some combination of the government and the private sector" backing the accounts.

The fact that one-fourth of consumers said banks should be required to extend certain services even at a loss indicates some people believe banks have a special responsibility.

"I think there's a feeling in a portion of the population that banks have deep pockets and [I'll] save my sympathy for the little guy in small business, not for the big corporation," said Fred Manning, a community affairs officer for the Federal Reserve Bank of Philadelphia.

Mr. Manning said that banks have done a better job of developing lifeline accounts in recent years but that they can do more. For one thing, he encourages banks to promote the growth of neighborhood credit unions geared for low-income consumers, especially in neighborhoods where commercial banks might have closed branches.

Supporting neighborhood credit unions gives a bank "a chance to regain some of the image that it lost by leaving," he said. "The hope is that the customers of the credit union can grow and then qualify for credit from the banking system."

The 'Unbanked'

Another finding from the *American Banker* survey was that only 2% of the respondents do not maintain any type of account at a financial institution. This figure is far below the 10% to 20% of the population that most previous research has said belong to "unbanked" households. The discrepancy can be explained by the fact that Trans Data conducted its research by telephone and could not reach low-income households without phones.

A study last year by the General Accounting Office, a research arm of Congress, showed that about 17% of the U.S. population did not have banking accounts. A Federal Reserve Board study in 1983 found that 21% of households did not have a checking account, the most basic of banking services.

With only 24 people in the Trans Data sample lacking an account, any conclusions based on their reasons for staying out of the system would not be scientifically valid. But they did make some revealing comments.

Nineteen members of this unbanked group said that at one time they had accounts with financial institutions. Nine of the 24 said they do not have accounts because they cannot afford them, and five indicated that they did not think banks were safe or trustworthy. Twelve of the 24 said they use cash to pay monthly bills, and 10 said they rely on money orders.

Many bankers contend that because of such attitudes, a significant portion of unbanked people would not sign up for a lifeline account no matter how affordable or convenient.

"Almost the same number of people who say they can't afford a bank account are using things like money orders that are actually more expensive," said Mr. Kolesar.

Cash Only Please

Mr. Paro of the ABA said his research has identified some people who prefer to operate in a cash-only world for reasons that range from "not wanting a paper trail for tax reasons" to "people who don't want their spouse to know what they make." Drug traders and other illicit businessmen also operate off the books and want to keep it that way.

But Mr. Fogarty of the New Jersey consumer group points to other research that shows rising bank fees, higher balance requirements, and branch closings in low-income neighborhoods are disenfranchising people from the banking system.

"All the people who use check-cashing outlets would use banks if banks were located in their communities," he said.

$15 Million Loss In Bad-Check Scam

By JEANNE DUGAN COOPER

American Banker

August 3, 1989

NEW YORK — Federal and local law-enforcement officials in four eastern states are investigating a fraudulent check-cashing scheme that they believe is one of the costliest on record, causing up to $15 million in losses for banks and retailers over four years.

Police in Montgomery County, Maryland, arrested the latest suspect Wednesday. They have also seized a "how-to" manual, prepared by the alleged criminals, which lists 10 banks that are said to be easy targets for fraud. (See story on page 10.)

Six people have been arrested so far on charges of passing thousands of stolen and fraudulent checks and credit cards issued by dozens of banks in New York, New Jersey, Maryland, Virginia, and Washington, according to several officials involved in the case.

The investigation began in April, when Montgomery County police arrested Richard Sears, 29, on charges of attempting to pay for merchandise with a bad check, according to Sgt. Harry Geehren, a Police Department spokesman. Maryland and Washington police believe Mr. Sears, a man of many aliases, is the leader of an extensive crime ring.

Since the initial arrest, 15 law enforcement agencies including the U.S. Postal Service, Federal Bureau of Investigation, and state and local authorities have gotten into the act. They are using the computer files of three major check-guarantee companies to track the bad checks.

But officials don't yet have a finger on the exact magnitude or cost of the crimes as new evidence, names, and complaints turn up constantly.

"The total keeps going up every day," said Detective Jerry Williams, who handled the case in Washington with Officer Nole Mueller. "There are thousands and thousands of checks involved. We'll have checks coming in for months. It's really mind-blowing when you sit down and start thinking about it."

He said one suspect confessed that the group cashed checks worth $5 million last year, drawn on about 20 different banks. Within the past five years, the group was responsible for $10 million to $15 million in bad checks, according to the suspect's account.

To indicate the scope of the scam, Mr. Williams noted that two of the people under arrest used 80 different names to open checking and credit accounts under false pretenses. Most of those were names of victims whose identification had been stolen.

The criminals would use those iden- [illegible] then would use the bad checks and cards faster than the banking system could catch up to them.

"This is the largest economic scam I can remember in my 22 years on the force," said Jack Scott, a former detective with the district attorney's office in Suffolk County, New York.

Mr. Scott now works for JBS Associates, a Ringwood, N.J.-based company that guarantees checks for retail merchants and banks. JBS has connected the ring with $750,000 to $1 million in losses sustained by its clients. TeleCheck Services Inc. and Telecredit Inc., competitors of JBS, are also cooperating with the investigation.

According to the ring's how-to booklet and official accounts, the group operated in the New York-Washington corridor by using stolen identificaton from one area to establish new checking accounts in another. Members of the group then purchased merchandise by check and sold it to fences who resold the goods.

After a while, members of the group would report their checks and credit cards stolen and create new identities. The scam started in New York about five years ago, officials say.

Police on the case in Washington recently discovered two houses that contained thousands of dollars worth of men's clothing, jewelry, and electronic equipment, and other merchandise believed to be obtained through check fraud.

All the furnishings and decorations in one house – including the kitchen cabinets, bathroom vanities, and a fancy wood front door – were paid for with bad checks, Mr. Williams said.

While police were in this house, a suspect arrived with more than $1,000 worth of men's clothing he had allegedly purchased with bad checks. He was arrested on the spot.

In another incident, Washington police said the members of the group threw a party for themselves and decided to do their own catering. With bad checks, they allegedly purchased $20,000 to $30,000 worth of food and catering equipment, including a crystal chandelier. Police recovered the equipment from storage in a Washington warehouse.

"According to the source I talked to, they had the party and they had a pretty good time," said Detective Williams. "We have obtained a full-color photo album of the party. There's no denying they knew each other. There they were, all the suspects, in a picture together." ■

Criminals List Their Favorite Banks

What is the easiest way to beat the security system at retail stores and banks? Just ask a criminal.

Mixed in with stolen goods seized by officials investigating a major fraudulent check-cashing ring in the Washington area were pamphlets prepared by the criminals to teach new recruits how to defraud banks and vendors.

The book listed 10 steps to check-cashing success and included lists of 10 easily duped banks and 10 retail stores of similar reputation.

The how-to manual advises: "(1) Get a N.Y.C. driver's license; (2) Get a Richmond [Va.] driver's license; (3) Open a mailbox in Richmond; (4) Open an instant [credit account] at Lord & Taylor; (5) Open an instant at Lane Bryant, (6) Open an instant at Kay Jewelers; (7) Open an instant at Bailey Banks & Biddle; (8) Open up N.Y.C. and Washington and Richmond bank accounts; (9) With the Richmond driver's license get a duplicate so that when you use one to get a D.C. license you still have the other one; (10) Open accounts with all licenses and turn it out."

The vulnerable financial institutions, listed with incomplete names, were Central Fidelity [Bank, Richmond]; First American [Bank of Virginia, McLean]; Citicorp; Riggs [National Bank of Washington]; Sovran Bank, Richmond, Va.; Perpetual [Savings Bank, McLean, Va.]; First National Bank of Maryland, and an institution called Citizen which was not described further. It may have been Citizens Savings Bank, Silver Spring, Md.

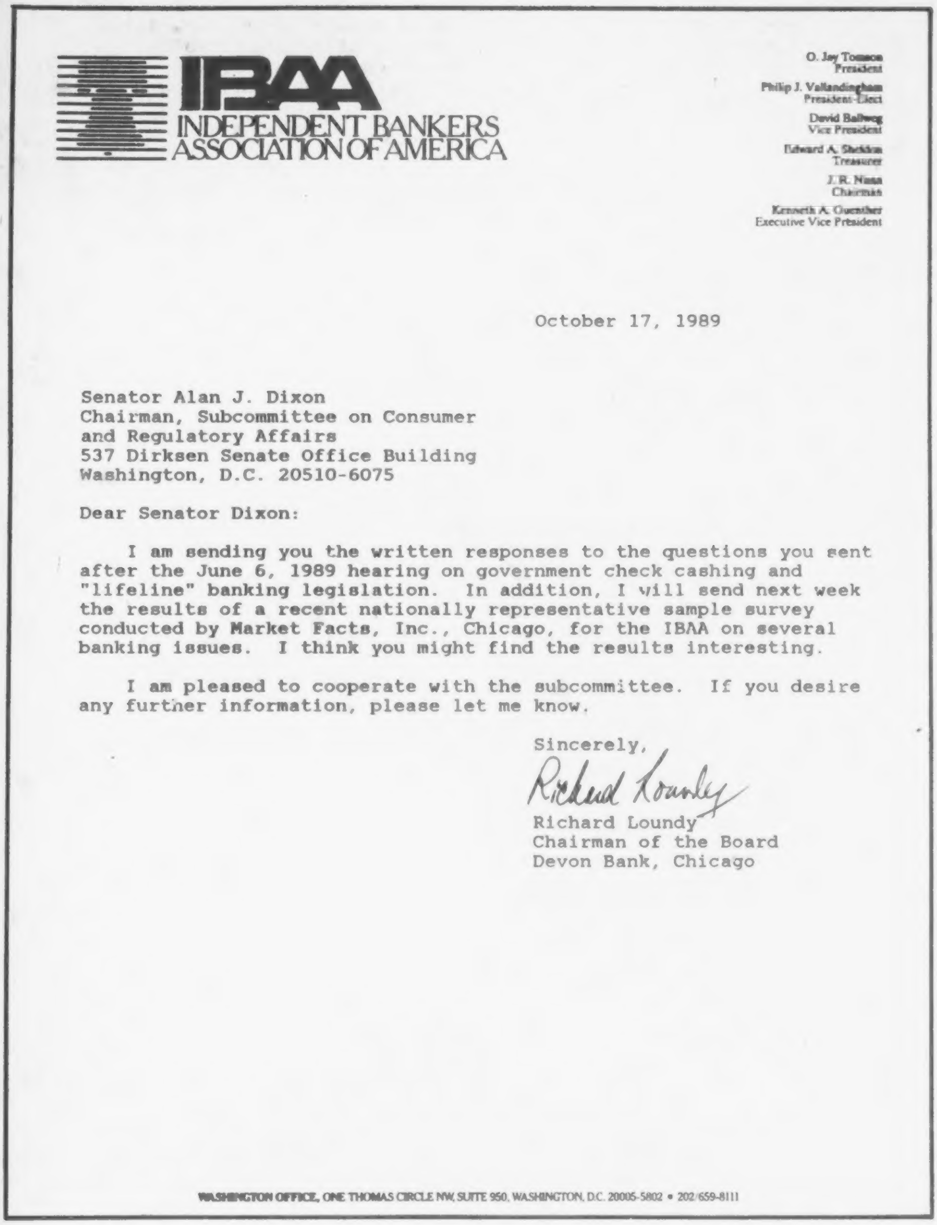
According to Detective Jerry Williams, who investigated the case in Washington, police are so busy with drug-related crimes and homicides that economic crimes like check fraud don't top the priority list.

"In the retail and law-enforcement community, there's not a lot of manpower devoted to economic crime," said Mr. Williams, who holds seminars to teach merchants how to avoid such crimes. "There's no way manpower can be devoted to fight this problem."

The detective said he is attempting to educate other law enforcers to the fact that economic crimes are usually related to drugs and violent crimes.

"I've interviewed hundreds of retail thieves," he said. "At least 90% do it to support drug habits. If we pull together and communicate, these types of problems will be less common. It all ties together. A lot of people are missing the point."

— Jeanne Dugan Cooper



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Kenneth A. Guenther
Executive Vice President

October 17, 1989

Senator Alan J. Dixon
Chairman, Subcommittee on Consumer
and Regulatory Affairs
537 Dirksen Senate Office Building
Washington, D.C. 20510-6075

Dear Senator Dixon:

I am sending you the written responses to the questions you sent after the June 6, 1989 hearing on government check cashing and "lifeline" banking legislation. In addition, I will send next week the results of a recent nationally representative sample survey conducted by Market Facts, Inc., Chicago, for the IBAA on several banking issues. I think you might find the results interesting.

I am pleased to cooperate with the subcommittee. If you desire any further information, please let me know.

Sincerely,

Richard Loundy

Richard Loundy
Chairman of the Board
Devon Bank, Chicago

WASHINGTON OFFICE, ONE THOMAS CIRCLE NW, SUITE 950, WASHINGTON, D.C. 20005-5802 • 202/659-8111

The following are the IBAA's answers to Senator Dixon's written questions on government check cashing and "lifeline" banking legislation. These answers are for submission to the hearing record of June 6, 1989, of the Senate Banking Committee, Subcommittee on Consumer and Regulatory Affairs.

Q.1. What provisions would be necessary to add to S.907 to adequately protect depository institutions against fraud?

A.1. The legislation should include language permitting a bank to require that government checks be deposited directly into an account. On page 2, paragraph 4, of our testimony, we say:

> "Direct deposit is a reasonable compromise between the concerns of the banking industry and those of the consumer. It is a safe and reliable way to deliver funds to the consumer while greatly reducing the risk of fraud to the bank. Direct deposit also provides benefits to the governmental agency issuing the funds, since it is less expensive and more efficient than issuing paper checks."

The Financial Management Service of the Treasury Department testified before your subcommittee indicating that the movement in the Federal government is toward electronic payments transactions such as direct deposit. On page 6 of their testimony, they say:

> "...electronic payment techniques such as direct deposit provide a far higher level of service in the areas of security, dependability, convenience, and early access to funds than do check payments. The only losers are those people who are in the business of stealing and forging government checks."

In addition, any single instance of fraud should be grounds to close an account. No bank should be required, as provided in the legislation, to tolerate a "pattern of fraud." Again, direct deposit into an account would clear up many of these problems.

Q.2. Page three of your testimony suggests that check cashing centers should be included in a review of the check cashing process for the underbanked. What specifically should be done with regard to check cashing centers? Should they be covered by S. 906? With what sort of amendments, if any?

A.2. Since it is the fees that these check cashing centers charge that cause so much controversy, Congress should examine them. Usury laws are set by the states, so it makes sense for Congress to compare those states which are not regulating check cashing centers with those that are. This would permit Congress to develop an appropriate legislative solution to the problem of inadequate regulation by some states.

Q.3. Page three of your testimony states that the size of an overdraft often is as important as the number of overdrafts. Explain why. Do you consider an overdraft to be an instance of fraud, as the context of the statement suggests?

A.3. The size of an overdraft is important because if someone overdraws their account by $5 or $10, it is likely to be inadvertent, while a $100 or greater overdraft is much more likely to be intentional. If you overdraw your account by $100-200, you get an unsecured "loan" which has really not been formally approved by the bank. This type of transaction can be considered fraud if it is performed intentionally. In fact, regulators look at overdrafts by insiders when they are looking for instances of insider abuse.

Q.4. Your testimony seems to suggest on page four that a low-income requirement be added to S.907. Describe your position in more detail.

A.4. IBAA retained Market Facts, Inc. to do a nationally representative sample survey on several banking issues (August 25-27, 1989). Analyzing this data, it became evident that someone who could afford an account could utilize this "lifeline" feature. The data showed that 19% of the population is "unbanked," meaning that they do not have a checking, savings, or money market account, IRA, or CD with a bank, S&L, or credit union. Of those consumers, 13% earn over $40K per year; 37% earn over $25K; 19% earn $15-25K; and only 44% earn less than $15K. This data indicates that at least half of the unbanked population earn sufficient income to have an account of some type. It is likely that those earning more than $40K do maintain an account, perhaps with a non-bank. We suggest that some sort of income test be required for access to a lifeline account. A requirement that a consumer receives public assistance might also be appropriate.

The IBAA survey data also showed that of the people that do have accounts, (82% of the population), 50.4% have less than $10,000 total in their checking, savings, IRA, CD or money market account. This could be interpreted to mean that the majority of accounts are low balance ones. These individuals would be able to take advantage of "lifeline" accounts under the definition in the legislation. Congress should think about what "low balance" means and who should qualify for a "lifeline account." A "needs test," similar to the needs tests currently used to qualify for many student or mortgage loans, should be developed to guarantee against the abuse of "lifeline" accounts.

Q.5. The Federal Financial Institutions Council issued a joint policy statement encouraging depository institutions to offer basic services and asking trade associations to monitor compliance. How are you monitoring compliance? According to the General Accounting Office only 18% of banks and thrifts offer a "lifeline" type account to the general public. Why are only 18% complying?

A.5. When the FFIEC issued its joint policy statement, the IBAA did a detailed supplement to the Washington Weekly Report newsletter, which reaches over 6500 community banks. I have enclosed this for you. However, the IBAA is a trade association and not a regulator. Banks join us for representation, services and information -- not for examination.

Several years ago, the IBAA itself did a random survey of about 25% of our membership. We found that over 40% of the banks surveyed had not increased fees in over five years, 78% offered senior citizens free services, 45% offered students free services, and churches, non-profit groups and civic organizations were frequently mentioned as other recipients of free services. Only one percent of the banks responding reported charging their customers for check cashing. Non-customers could cash a government check for free at 68% of the banks.

Moreover, some of our banks may refuse to cash benefit checks for non-customers but offer the recipient the option of opening a low-cost checking account. Other banks offer the unbanked benefit recipients a free checking account if they sign up for direct deposit.

This data does not support the GAO figures and indicates that many banks, especially the smaller ones, are complying with the FFIEC request.

Q.6. Should everyone have a checking account? What are the most effective means to meet that goal?

A.6. Everyone who wants access to a fairly priced account should receive it. However, not everyone wants a checking account. The government shouldn't require consumers to open an account if they do not wish to have a relationship with a financial institution. The key is availability of service, not requirement. A decentralized, diversified financial system should be maintained to keep competition strong in this area.

QUESTIONS FOR JOHN P. KELLY, JR. FROM SENATOR ALAN J. DIXON JUNE 6, 1989

Q.1. Describe the asset size of your members.

(1) In regard to the asset size of our members, as of December 31, 1988, our member banks range in size (total assets) from $8.7 million to $807.9 million, for an average size of $74.5 million.

Q.2. Should everyone have a checking account? What are the most effective means to meet that goal?

(2) Regarding your question on whether everyone should have a checking account, our testimony made reference to several surveys which indicated that not everyone wanted to have a checking account, and we concur with those results. We believe that the present financial payments system should and does provide for the fundamental needs of society and the movement to an electronic delivery system would be the most efficient means to meet the needs of virtually all Americans, without the need to have a "checking account".

Q.3. If cheaper services are already available at banks than at check cashing centers, why do so many people use the significantly higher priced centers?

(3) In regard to those persons who choose to use significantly higher priced check cashing centers, it should be noted that many people choose an institution to meet their financial needs based purely on convenience of location and business hours. In light of the increasing number of bank and branch closings in many urban communities, many individuals no longer have the option to utilize banks for their financial needs. Conversely, check cashing centers are often conveniently located in those areas to take advantage of the great need for their services.

Q.4. In what percentage of checking accounts at your member banks do customers write ten or fewer checks per month?

Q.5. What is the typical range of fees on a no minimum balance banking account at your member banks? What is the typical range that a person would spend per month at a check cashing center?

Questions numbered (4) and (5) cannot be answered without first conducting a survey among our membership. Unfortunately, the NBA neither has the manpower nor the financial base to conduct such a survey and submit the answers to these two questions in a timely fashion. I would be, however, more than happy to work with you and other members of the Subcommittee on fashioning legislation that takes into account the unique mission of minority and women-owned banks in this country of providing available and affordable financial services to their predominately minority, low-income, inner city communities. The very communities often abandoned by other institutions, many of whose activities created the impetus for the issues subject to debate at the June 6, hearing.

AARP RESPONSES TO QUESTIONS FOR THE RECORD
JUNE 6, 1989 HEARING ON
BASIC BANKING, GOVERNMENT CHECK CASHING

Q.1. The Connecticut Superintendent of Banking testified that the Connecticut free government check cashing law had not increased the number of people using banks and thrifts versus check cashing centers. Do you believe the national experience with S. 906 would be different from the Connecticut experience? Is there a more proven way to attract the underbanked back into the banking system?

A.1. The key to the success of S. 906 is to let people know they have an alternative to check cashing centers. AARP would hope that once S. 906's protections were in place, un-banked people would recognize the low-cost option banks would represent, and would seriously re-evaluate their continued usage of the more expensive, check cashing centers. To help accomplish public awareness of this new option, AARP would not be adverse to delegating to the Federal Reserve Board the responsibility for devising a scheme designed to communicate S. 906's protections to its intended constituency. While the posting of signs in bank windows and lobbies may be helpful to some, outreach efforts to nutrition and public housing sites, etc. should also be considered. Questions of adult illiteracy and language barriers must also be addressed. Public service radio announcements would also help to advertise the availability of check cashing services at financial institutions. An aggressive, public education/ marketing campaign by the government, financial institutions and consumer advocacy groups would also help to assure the success of the program.

Since S. 906's goal is to bring the un-banked back into the banking system, the bill should not contain requirements which potential government check cashers might consider burdensome. This is one of the primary reasons for AARP's opposition to the mandated use of direct deposit. Given the aversion of low income and older persons to use direct deposit, we fear mandating its use would result in the failure of many who would benefit from S. 906 to utilize the services required under S. 906.

Q.2. Does the American Association of Retired Persons believe that the federal government should require depository institutions to offer services on which they will lose money? on which they will make zero profit?

A.2. AARP believes financial institutions have an on-going responsibility to respond to the credit and depository needs of the local communities in which they are located. AARP has never advocated that financial institutions should be required to subsidize or offer services on which they would lose money. Since the Federal Reserve Board, under S. 906, is charged with the responsibility of setting a reasonable fee for government check cashing services, neither subsidization nor loss of money would result under the bill. The financial institution would be free to charge up to the Fed's reasonable fee, which would take into consideration all financial institution costs for providing the service. AARP believes the financial services industry's concerns about losing money and subsidization under S. 906 to be illusory arguments.

A much larger subsidization question--are taxpayers subsidizing current banking practices--arises out of the value to financial institutions of direct deposit. As AARP pointed out in its testimony before the House Consumer Affairs and Coinage Subcommittee on October 17:

> "The overall loss of earning potential for the government (under direct deposit) represents an attractive windfall for the banks, which would be free to invest these directly deposited funds before they are withdrawn by consumers. As the result of the tremendous infusion of cash each month under a direct deposit system, financial institutions would have the potential for reaping huge profits by investing funds from customers' accounts."

AARP's comments further estimated that the loss to the government, and windfall to the financial services industry, of the direct deposit float, is approximately $1.43 billion for retired worker Social Security beneficiaries (a limited category of government benefit recipients).

In response to the question, "Who's subsidizing whom?", AARP asserts that the value to the financial services industry of direct deposit should be viewed in tandem with their interest in promoting the use of mandated direct deposit. AARP further queries:

(1) Why has the federal government embarked upon such an ambitious direct deposit program when it is costing the government money?;

(2) Who is watching the float?; and

(3) Is Congress aware of direct deposit's drain on the U.S. Treasury?

CFA Consumer Federation of America

October 26, 1989

Dear Senator Dixon:

The following are responses to your questions for the record on the hearings on June 6, 1989 which were held on the issue of government check cashing and basic banking services.

Question 1: Yes CFA disputes the American Bankers Association statistics. We choose to use the GAO statistics provided in their 1988 check cashing report which were drawn from the Census data. This data states that about 17 percent of the 92.9 million families in this country have no account relationships with financial institutions. GAO points out that the difference in this statistic and that of the Federal Reserve Board, which is roughly half that number, could simply be based on such reasons that the Census survey involves going to each home, where the Federal Reserve survey used telephones. Furthermore, the Census definition of family were those related by blood or marriage where the Federal Reserve includes all families under one roof as one family.

Many low income families must share homes and many do not have telephones, so we believe that the Census figures are closer to reality, though probably still low. Furthermore, the results that have come in from different states, New Jersey, Virginia and California verify the Census figures with their own results. Therefore I am comfortable in the GAO statistics which are double the ABA statistics.

We see that there are many problems in the issue of encouraging people to use our financial system. Availability of affordable services is the problem we feel must be addressed first. Without addressing availability, you cannot address cultural or educational problems. Many people cannot afford accounts. Many people choose not to have accounts due to affordability, lack of understanding how to operate a checking account, previous treatment in banks, poor banking hours, lack of availability due to location of bank branches.

S. 906 and S. 907 address availability. This is step one. Without such availability we cannot begin to use effective educational or

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marketing tools, because the accounts are not available anyway.

Question 2. The range of fees differs in many states and by bank. According to our fifth annual bank fee survey, on accounts that are low-balance checking accounts, fees averaged $4.40 and ranged as high as $10 per month with an average annual cost of $102. Fees at a check cashing center range from 1-6% for government checks, meaning that a person cashing 12 government checks a year would spend $120-$300 per year. Money orders would cost an additional amount. We assume an average of four money orders a month, at an average cost of $25.15 a year.

Question 3. I have no statistics to base any different reaction to a national situation if it was like that created in Connecticut due to their check cashing requirements. The only thing that might influence a change from a national perspective would be the full attention and support services of national organizations in terms of outreach and efforts to bring their members into the use of such a system. For instance, AARP, CFA, ACORN and others would be working with their members to alert consumers to the availability of the service.

Still, we have pointed out that a necessary and useful addition to this legislation would be language establishing marketing, educational and outreach programs on financial services targetted to low and middle income. Such education and outreach would be very useful to bringing consumers up-to-date on the new financial products while it serves as a tool in bring more low income back into the system.

Question 4. We do not believe that banks should be required to lose money. We only caution in the judgement of when banks are actually losing money. The language in the legislation which refers to fees that take into account all net processing costs is quite important because it refers to the methodology of including all profits from investments of deposit funds in the overall calculation of costs of accounts. We do not believe that depository institutions should be forced to perform a service that causes them to go broke. Therefore, the fee setting should include all costs based on actual cost studies. We do not have a problem with zero profit calculations, since we believe that the banks will be covering all basic costs including administrative costs in such calculations and so that means that salaries are covered also. The basic tenet of such services are predominantly public service in their orientation and so would seem to fit with a zero profit calculation methodology. Correspondingly we would not oppose the inclusion of a small profit if necessary for an incentive.

Thank you for your time.

Sincerely,

Peggy Mill

Peggy Miller

QUESTIONS FOR MARTHA R. SEGER FROM SENATOR ALAN J. DIXON JUNE 7, 1989

Q.1. Page nine of Consumer Bankers Association's testimony describes how S. 909 could be interpreted to require banks to comply with each of the twelve assessment factors. Does the Federal Reserve Board expect compliance with all twelve of the assessment factors?

Page nine of the Consumer Bankers Association's testimony describes how S. 909 could be interpreted to require banks to comply with each of the twelve assessment factors. Does the Federal Reserve Board expect compliance with all twelve of the assessment factors?

Yes, but in a limited sense. As made clear in the uniform interagency CRA rating system (copy attached), CRA examiners rate performance in five performance categories -- Community Credit Needs and Marketing, Types of Credit Offered and Extended, Geographic Distribution, Discrimination or Other Illegal Credit Partices, and Community Development and Other Factors -- which represent groupings of all twelve assessment factors set out in the regulation implementing the CRA. Thus all twelve factors are reviewed.

Yet it is not really correct to say that we expect banks to "comply" with each of them. Each assessment factor is reviewed and taken into account under one of the five performance categories, but we do expect that banks will exhibit varying levels of activity under the factors for reasons that reflect the credit needs of its community, or the bank's expertise and business orientation.

For example, a bank may choose not to participate in governmentally-insured, guaranteed, or subsidized loan programs for housing, small business, or small farms, even though participation in such programs would be considered under the tenth assessment factor which calls for the review of these activities. Examiners may conclude, in light of the bank's performance under the other assessment factors that are weighed in this category, that the bank is doing a satisfactory or even outstanding job under the category. This would be the case if, for example, examiners found that the bank lacked the expertise to participate in such programs, or that the bank's efforts to ascertain local credit needs revealed that a need for federally-assisted mortgage credit simply did not exist in the community, or was already fully addressed by other institutions. Examiners might also have found that the range of conventional loan products offered by the bank was on target in responding to local needs for credit. The point is that examiners focus on the totality of efforts made within each grouping of factors that constitute the performance categories, rather than on single factors independent of each other.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MA .A R. SEGER
MEMBER OF THE BOARD

July 21, 1989

The Honorable Alan Dixon
Chairman
Subcommittee on Consumer and
  Regulatory Affairs
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

During the June 7 hearing on the Community Reinvestment Act (CRA), before your Subcommittee on Consumer and Regulatory Affairs, you requested the Federal Reserve's specific comments on the provisions in Senator Metzenbaum's bill, S. 909. I am pleased to provide the following response.

The Board supports the general concept of requiring regulatory agencies to prepare and publicly disclose written evaluations of institutions' CRA performance. We believe that this would be fully consistent with the thrust of the CRA policy statement issued in March by the four federal financial institution supervisory agencies, and would promote the early start of a constructive dialogue between an institution and members of its community about its CRA record.

However, the CRA evaluations that we support would *summarize* the examiner's findings and conclusions, and would provide supporting information related to the CRA assessment factors. They would *not* be the same as the examination reports themselves. Nor would they divulge material from the examination report which must be treated confidentially--such as information about the financial condition of the institution, and any sensitive information about its employees, customers, or members of the community.

Senator Metzenbaum's bill, however, can be read to require the agencies to make public the examination report itself--not a summary. Additionally, the bill sets out criteria for information that *can* be included in the confidential section of the report and further prohibits disclosure of this information to the depository institution or the public except in unusual circumstances. The Board opposes these provisions because we believe it is important to effective supervision and communication that examiners have a separate and confidential avenue for conveying the facts and conclusions of their reviews to the institutions.

The Board also opposes disclosure of institutions' numerical CRA ratings, as required in S. 909. At the very least, release of the numerical rating would divert attention from the more important and thorough information contained in a narrative summary of the examiner's findings. The rating systems for examinations were developed as a supervisory shorthand to enable us to know which banks need closer attention. The rating is not self-explanatory and, more importantly, we believe that there is also a potential for undermining public confidence in the safety of deposits in an institution if an adverse CRA rating were to be misunderstood as a reflection on that institution's financial soundness. In our view we can accomplish the purpose of this provision and avoid this risk by publishing a summary assessment of an institution's performance under the CRA.

Finally, the Board opposes the requirement in S. 909 that CRA evaluations be focused on three specific types of credit--loans for low and moderate income housing, small business, and small farms. Such a requirement is inconsistent with the Community Reinvestment Act, which does not require any specific type of lending. Since communities and banks differ, and because many other lending activities can contribute to community revitalization, we believe it would be unwise for the statute to place primary focus on a few enumerated types of lending.

I hope this information is helpful to your Subcommittee. Please let me know if I can be of further assistance.

Sincerely,

Martha R Seger

QUESTIONS FOR CHARLES H. GRICE FROM SENATOR ALAN J. DIXON
JUNE 7, 1989

Q.1. "Recommendation 3" of your testimony stated that secondary markets, standardized underwriting criteria for CRA-type loans, and credit enhancement mechanisms are essential to increased CRA lending. What specifically should Congress and/or other parts of the federal government do to improve these three avenues for increasing CRA lending?

1. Ask FNMA, GNMA, FHLMC et al what they would do if you required them to devote one percent of their loan volume to low and very low income housing loans.

2. Ask FNMA et al to identify the impediments to greater securitization of these loans, and how they would recommend overcoming these impediments.

3. Authorize pilot projects, like the mortgage banking program joint ventured between five San Francisco banks and the Low Income Housing Fund, to make interim loans to community-based developers of truly affordable housing for low and very low income persons. CRI & LIHF are proposing to carry this concept to other cities and regions now. Such pools and relationships between lenders and community development loan funds are essential to getting affordable capital to quality developers, and therefore to achieving the "volume" necessary to establishing a healthy FNMA-style (i.e., formal) secondary market .

4. FNMA is the key to ERISA; and ERISA is the key to the pension funds; and the pension funds are the key to creating affordable housing in volume.

FNMA has got to develop more flexible underwriting, but FNMA is concerned that these securities must be discounted (goring someone's ox, in the current setting) one or two points and therefore will be unsaleable. Worse, they fear a reputation for selling "below investment grade" securities. FNMA is a benchmark of quality under ERISA, the arbiter of what the "prudent investor" would buy.

Congress could change ERISA to permit (or require) fund managers to make (an undefined level of) socially desirable investments, though they may yield less than market rates. The result might be creation of a lower-yielding class of FNMA securities that are "prudent" but saleable en mass.

ERISA now obliges profit-maximizing behavior by pension fund managers, who are FNMA's biggest customer. Fund managers may invest in junk bonds, but not in FNMA Affordable Housing Loans, which may yield one or two points below market, or have more flexible terms or structure). Fund managers can be sued for buying lower-yielding but more socially valid investments that still make a profit.

A secondary market relies on volume, and pension funds are the key to that volume. Between the Funds and the volume stands FNMA, which is impeded by ERISA.

5. Another partial answer to the secondary market problem is extending CRA obligations to cover insurance companies, which hold most of the long-term commercial, industrial and retail mortgages in the country today, and the securities firms and money market mutual funds that are major forces in real estate and business development finance.

Insurance companies often have reinvestment obligations under state law, enforced by insurance commissioners, but these are very uneven in approach, coverage and enforcement.

6. Private mortgage insurers should perhaps have CRA obligations. GE Mortgage Credit in Raliegh NC is developing a product that may be helpful in this regard, and you should hear from them. They would offer PMI at a discount on loans for lower income or first-time borrowers on several conditions, including 10 hours of basic banking and homeowner education and acceptance of a basic home-maintenance inspection contract. GEMC will accept a higher ratio of debt service to income from these buyers than is customary (up, from 28% to 33%) and forego any concern on the source of downpayment (normally a lender requires assurance that the downpayment is not a loan). I recommend you talk with GEMC about why they did this, how they see the market, who their competition is (or isn't).

CBA
CONSUMER BANKERS ASSOCIATION *The Association for Retail Banks and Thrift Institutions*
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October 27, 1989

The Honorable Alan J. Dixon
Subcommittee on Consumer and Regulatory Affairs
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, DC 20510

Dear Senator Dixon:

This letter is a response to your request for additional information concerning my June 7, 1989 CRA testimony before the Subcommittee. Both the Consumer Bankers Association and I appreciate the opportunity to participate in these important proceedings.

Q.1. Provide details about your recommendation for mandatory interagency uniformity with respect to data gathering and reporting requirements, as set forth on page eleven of your testimony.

Answer: The absence of consistent examination standards and results as between the respective agencies have been criticized by both industry and public interest groups alike. The differing approaches of the agencies in this area have been chronicled in hearings before the Subcommittee on July 31, 1989 and October 24, 1989 ("agency hearings").

The absence of a consistent approach to CRA oversight is a function of a number of factors, including (i) the ambiguous mission statement in the statute and regulatory guidelines, (ii) differing regulatory organizational structures, and (iii) differing levels of sophistication and expertise within the respective agencies.

For understandable reasons, it has been and will forever be difficult to conceive of a standardized list of CRA performance criteria because community needs differ from place to place. It is far less difficult, however, to envision a cadre of CRA examiners organized, trained and generally operating in some degree of concert on CRA issues in each of the respective agencies.

To an extent, the agency hearings suggest some interagency acknowledgement of the virtues of this approach and actual movement in this direction. These developments are to be applauded and encouraged. The interagency policy statement on CRA also exemplifies movement toward a uniform approach facilitating compliance.

Notwithstanding these positive developments, however, frustrating and confusing pronouncements continue to confound industry efforts in this respect. At a recent banking compliance conference in Washington, D.C., Ron Zimmerman, a vice president at the Atlanta Fed surprised attendees by stating that "geocoding" of CRA loan activities was expected by his bank's examiners. Based on conversations with bankers from other Fed districts, it is not at all clear that this is a system wide expectancy, let alone a uniform interagency approach.

For example, at the same conference, John McDowell, director of OCC consumer activities, said that although a recent OCC Atlanta office advisory "strongly urged" the practice, "... (a) banker doesn't have to do it, but without that it's very difficult to know how you're doing." And Janice Smith, director of consumer affairs at the FDIC said "...(I)t's not required, but it doesn't hurt to do it," while an examiner from the FDIC's Dallas office pushed for it, especially in situations involving consumer group complaints (see attached FERC Report excerpt).

This is a microcosm of the problem to which we have alluded. Greater interagency coordination in CRA oversight must be institutionalized through joint training, on-going consultation, promulgation of comparable examination procedures and dedication of similar staffing resources. In this latter regard, specially trained personnel focused primarily on CRA lending may be a useful step. Until then, a good effort in Seattle may not be a useful standard for Springfield and so on.

Q.2. Provide further examples of how risk-based capital standards may penalize CRA-type lending and details of how appropriate capital standards could be designed for certain types of CRA loans.

Answer: Our suggestions concerning risk-based capital focused on the disincentive to experiment in innovative and untested forms of lending inherent in such a capitalization scheme. CRA lending, therefore, is not so much "penalized" as it is placed at a comparative disadvantage with other, perhaps more profitable activities that require the same capital reserves.

The institution of a risk-based system of capital requirements inevitably rewards prudence (i.e., conservative investment activity) and penalizes risk (i.e., unconventional investment activity). The object of the system is, after all, to reign in the tendency to use publicly owned and insured funds in ventures lacking a track-record of performance or some assurance against loss (such as a form of guarantee). The instrument for achieving this goal is the requirement of an additional investment of private capital by the venture's promoter to backstop the perceived increased risk.

For example, non-secured credit card loans require the maximum capital reservation or, in the parlance of the capital formula, a "100% risk weighting." This is twice as much retained capital as is required of a similar dollar amount of residential mortgage loans. Government guaranteed student loans require only 1/5 of the retained capital required for credit card loans. The historical performance and policy objectives of these latter credits, as well as the security of the real estate mortgage and/or federal guarantee, are perceived to lessen the attendant credit risk and justify favored treatment.

In a sense, the CRA and housing related success stories which have received the Subcommittee's attention in recent months cannot be readily integrated into this system of capital requirements. As it stands, such loans would generally receive the same capital treatment as credit cards, unless specifically devoted to residentially secured housing. This is not necessarily a function of their inherent riskiness - indeed, great effort and care is invested in their financial underpinnings to insure against undue risk. Rather, it is a function of their complexity, uniqueness and varying profitability.

First, these are often highly unconventional transactions matching state and local investments, tax breaks and community circumstances with revolving loan commitments in varying amounts from a consortium of lenders. The transactions are negotiated on a case-by-case basis, involving representatives at several government levels, community development professionals, lender representatives and public interest groups. Generic risk-weighting in this light seems difficult, at best.

Second, since no two transactions are alike, their historical performance establishes no clear track record for purposes of integration into the risk-based capital framework. Once again, quantifying the associated risk and profitability of each transaction on a case-by-case basis is not feasible under existing capital rules.

A better course may be to focus on desirable policy objectives and accord favorable capitalization treatment to compliance with those objectives. For example, a reduction of capital requirements might be legislatively mandated for investment dollars devoted to a particular type of venture (e.g., small business or residential or multi-family housing construction or rehabilitation of a type and in an area certified as desirable by state or local authorities). More generally, a "credit" against overall capitalization requirements might be made available under such circumstances (e.g., 10-20 basis points across the board for achieving a certain dollar volume of desirable investments).

These approaches would encourage operation of market forces without placing the onus on the federal government of mandating uniform investment rules for different communities or specifying particular results. Lending institutions would be free to take advantage (or ignore the implications) of these incentives. Coupled with other positive incentives alluded to in our testimony, we would be surprised if this approach did not have an immediate and salutary effect.

I hope the foregoing has been responsive to the Subcommittee's request. I would be pleased to answer any questions or provide any additional information deemed necessary.

Thank you again for your consideration in this matter and that of your staff.

Sincerely,

John Kolesar

John Kolesar
Chairman, Government Relations
Council

~~related to the 1099s. The bank's lending officer also expressed concern about the recordkeeping burden of the proposed small business amendment to Reg B.~~

~~The president of the largest community bank in the group, $125 million, which was criticized in an exam because its Fair Housing logo in recent advertising was 1/4" square instead of the required 3/8", is so fed up with regulations that he wants to rescind his "HUD approved" status, the study notes.~~

~~A $22 million bank, which estimates it spends $18,000, or 4% of average pre-tax income on indentifiable compliance costs, is attempting to limit its liability associated with compliance errors by restricting its products. The bank doesn't offer variable rate home equity loans. And a $19 milllion single-office bank only offers loans that can be supported by its Laser Pro software.~~

"Geocode" Your Loans for CRA Compliance?

Now regulators are agitating for "geocoding" your loans, which means conducting a geographic analysis of loan data to ensure compliance with CRA. "Is geocoding expected? Yes," Ron Zimmerman, vp at the Atlanta Fed told stunned bankers attending ABA's national compliance conference last month at the Washington (D.C.) Hilton Hotel. There's been no regulatory mandate...yet.

But OCC's Atlanta office, in a recent letter to national banks, "strongly urged" them to geocode, says John McDowell, director of consumer activities in Washington, D.C. "A banker doesn't have to do it, but without that it's very difficult to know how you're doing," he says. Many bankers foresee expensive hassles.

The FDIC is taking a softer approach. "It's not required, but it doesn't hurt to do it," says Janice Smith, director of consumer affairs at the FDIC, Washington, D.C. But even FDIC examiners are pushing for geocoding if there are any complaints against your bank. "If we have complaints from a consumer group, then we have to geocode," says Eugene Peterson, review examiner at FDIC's Dallas office.

NAFCU
NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS
P.O. Box 3769 Washington, DC 20007
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June 5, 1989

The Honorable Alan Dixon
Chairman
Subcommittee on Consumer and Regulatory
Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing to you on behalf of the National Association of Federal Credit Unions, the only national organization exclusively representing the interests of credit unions chartered by the federal government, regarding consumer banking legislation. I understand that the Subcommittee will hold hearings on June 6 and 7 on two consumer banking bills introduced by Senator Metzenbaum: the Government Check Cashing Act of 1989, S. 906 and the Basic Banking Services Access Act of 1989, S. 907. I request that this letter be included in the Subcommittee's official hearing record.

The nation's credit union community is most supportive of this legislation's underlying objectives because they are inherent to the credit union mission. From their very genesis, credit unions have been in essence consumer organizations. Credit unions typically arose out of the frustration of individuals who could not find credit opportunities and a favorable return on savings at commercial financial institutions. Instead, they pooled their resources to meet the borrowing and savings needs of their communities. Not only were credit unions established to provide the essential financial services to their members that commercial institutions could not or would not provide, but they were structured as democratically-controlled, volunteer-directed cooperatives to guarantee that the credit union's members could determine for themselves what those services would be.

The credit union community has remained true to the founding ideal of "people helping people" to this day. While the minimal financial services needed to exist in modern society are far more extensive than they once were, credit unions continue to serve their members effectively and inexpensively. Thus, it is not surprising that in every consumer survey we know of, credit union services receive far higher grades than those offered by banks or savings and loan associations. For example, a Consumer Reports survey on checking accounts released last summer found that over 90 percent of respondents found credit union share draft accounts to be efficient, whereas only one out of three respondents found their bank or savings and loan checking account could be similarly characterized.

It is important to note that Congress granted credit unions the authority to offer transaction accounts less than ten years ago. Since then, approximately 37% of our nation's federal credit unions (3100 credit unions) have taken advantage of this authority to provide this service to their members. However, nearly two out of three federal credit unions do not offer share draft accounts today because either the limited size of the credit union does not allow for the prerequisite manpower and technology, or the members of that credit union determined for themselves that they did not want their credit union to offer that service. Similarly, a significant proportion of federal credit unions have no cash operations whatsoever.

NAFCU is pleased that both S. 906, the Government Check Cashing Act of 1989, and S. 907, the Basic Banking Services Access Act of 1989, recognize these important characteristics of credit unions. These two bills taken individually or in tandem provide for a financial services account to meet the needs of low and moderate income families. S. 906 provides for a government check cashing service, whereas S. 907 provides for a basic transaction service which allows up to ten withdrawals per month. Providing these services is not objectionable to the credit union community. To the contrary, these are precisely the type of consumer-oriented services that credit unions are expected to provide, and most which have the capacity are already doing so. For example, in the case of basic transaction services, the data cited earlier indicates that the vast majority of credit unions which offer share draft accounts are currently meeting the criteria contained in this legislation.

However, there are a significant number of credit unions which simply lack the wherewithal to offer share draft accounts or to operate on a cash basis. Many of these credit unions, if forced to offer a basic transaction service account, would be either confronted with huge start-up costs which would severely restrict the established services which the credit union's members have themselves selected or be forced to close their doors.

S. 906 and S. 907 as introduced by Senator Metzenbaum respond appropriately to these credit union concerns. Section 2(h) of S. 906 imposes the government check cashing service only upon credit unions which cash checks in the ordinary course of business, thereby accommodating those credit unions which do not operate with cash on hand. Likewise Section 2(d)(4) of S. 907 would require only depository institutions that maintain transaction accounts in the ordinary course of business to offer the basic transaction service, thereby excluding credit unions which do not offer share-draft accounts.

Furthermore, both S. 906 and S. 907 respect credit unions' common bond requirement. By law, federal credit unions are only allowed to serve individuals who fall within a defined field of membership (12 U.S.C. 1759). Both pieces of legislation accord full recognition to this legal restriction. Section 2(g) of S. 906 restricts government check cashing services to credit union members; likewise, Section 2(c)(1) of S. 907 requires that credit unions offer the basic financial services account to their respective members. It is for all these reasons that NAFCU supports the principles underlying this legislation to provide for basic, low-cost financial services.

On behalf of the entire association, I wish to congratulate you upon your ascension to the Chairmanship of the subcommittee. Mr. Chairman, in your eight years in the United States Senate, you have had ample opportunity to assess the character and vitality of the nation's credit union community. We are deeply gratified by the strong working relationship NAFCU has enjoyed with both you and the members of your very capable staff. As your chairmanship commences, NAFCU pledges its support to work with you on the issues before the subcommittee, and stands ready to be of assistance to you in any way. I thank you for your consideration of our views on this important legislation.

Sincerely,

Robert A. Hess
Chairman

RAH:SAS:ph

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The Honorable Alan Dixon
Chairman, Subcommittee on Consumer and Regulatory Affairs
Senate Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

On June 6 and 7 the Subcommittee on Consumer and Regulatory Affairs held a hearing on S. 906 the "Government Check Cashing Act of 1989." The Electronic Funds Transfer Association would like to comment on the legislation and requests that this statement be made a part of the hearing record on the subject.

The Electronic Funds Transfer Association ("EFTA") is the only national multi-industry organization committed to addressing the broad range of issues affecting the rapidly evolving EFT field. The Association's members include large and small commercial banks, thrift institutions, credit card companies, credit unions, department stores, oil companies, data processing firms, equipment and software manufacturers, telecommunications companies, and shared EFT networks.

During the subcommittee's consideration of legislation to mandate check cashing services for recipients of government checks, the EFTA recommends that Congress consider the use of electronic funds transfer (EFT) systems as a viable alternative to paper checks. As you may know, electronic systems involving direct deposits of federal entitlement payments, combined with systems for automated teller machine (ATM) or point-of-sale (POS) withdrawals using access cards, have been successfully tested and are now being used to an increasing extent.

EFTA strongly endorses efforts to increase the use of electronic payment systems and services. The Association believes the increased use of new payments systems technologies will bring significant benefits to the public, businesses and government. Such benefits include lower costs, greater operating efficiencies and more user convenience. In addition, EFTA believes that electronic systems can deliver new products and services that cannot otherwise be provided with paper-based systems. For these reasons, EFTA encourages Congress to consider the many benefits of direct deposit of federal payments combined with ATM and POS terminal access to cash in developing a solution to the government check cashing problem.

Currently, a number of EFT initiatives are taking place in the federal government in recognition of the costs savings and benefits of EFT. EFTA has recently concluded a research project which reviewed the current and likely future EFT activities of the federal government. The research project examined the various EFT activities of government entities and evaluated the potential opportunities for continued growth in these payment system technologies.

Electronic payments are more efficient, convenient and less costly than paper checks. The specific major benefits of direct deposit of federal entitlement payments (as an alternative to a check cashing program) with ATM withdrawals include the following:

For Recipients

1. A safer, surer way than checks to guarantee that funds have been deposited;
2. Faster funds availability because there are no check hold periods and no teller lines; and
3. Convenient access to deposited funds via ATMs.

For the Government

1. The Treasury Department estimates savings of over 30 cents per transaction in processing costs alone compared to check issuance.
2. Eliminates claims of lost, stolen and fraudulent checks. In FY 1987, Treasury reclaimed or refused payment on checks valued at $63.7 million.
3. Improved efficiency and financial control.

For Depository Institutions

1. Reduced costs of bad check losses.
2. Lower processing costs.
3. Improved customer relations.
4. Reduced lines on paydays.

Electronic funds transfer of direct deposits for federal recurring payments has been in use for over a decade. In 1980, 10.3 million, or 31 percent of the monthly Social Security payments, were directly deposited. By 1987, participation had increased to 46 percent. The proportion of Social Security beneficiaries accepting direct deposit is expected to increase dramatically as the Social Security Administration delivers benefit payments electronically. Applicants are, however, allowed to specifically request paper checks.

It has not always been easy to gain acceptance of direct deposit. One reason is insufficient education on the benefits of direct deposit to consumers. Another reason is that some banks and thrift institutions have been unwilling to accept certain direct deposit payments because they are held liable for withdrawals made from deceased recipients' accounts, even if the government fails to promptly notify the depository institution that the individual died (in FY 1987, checks valued at $38.9 million were issued by Treasury to deceased payees). Yet another reason has been the limited availability of locations to obtain cash.

Today, many of these problems are being solved. Attached is a set of data charts showing the growth of EFT transactions, terminals and cards. These charts illustrate the increasing acceptance and use of electronic payment systems by consumers.

In addition, the EFTA and the American Association of Retired Persons (AARP) are currently conducting a joint research project to analyze EFT and the mature consumer. The project will determine the degree to which individuals over 50 years of age use electronic funds transfer services, how EFT services are perceived, what the barriers are to their use, and what steps are needed to overcome any barriers. The results of the research project should also help to determine what educational and information services regarding EFT need to be provided to this important group. The research project is expected to be completed within several months.

Finally, the Financial Management Services division of the U.S. Treasury department is working closely with the EFTA and other private sector groups as well as consumer groups to discuss issues surrounding electronic benefits payments in an effort to further advance these programs.

Overall, electronic payments systems will afford the following benefits:

- Facilitate immediate, low cost cash access to pre-deposited funds for the needy who do not have regular bank accounts.
- Provide convenient access to cash at ATMs -- often at the points of greatest consumer need -- branches, supermarkets, shopping centers, bus and rail stations, and other locations. (There are more than 70,000 ATMs nationwide.)
- Eliminate problems of lost checks and checks stolen from mailboxes and postal delivery employees.
- Eliminate complaints of non-receipt of checks with associated investigation costs and delays.
- Resolve errors more quickly.
- Eliminate check fraud losses and reduce fraud losses from forged or invalid ID cards.
- Reduce long lines at branch teller windows.
- Save the Treasury and taxpayers money.

In addition to U.S. Treasury and other federal agency electronic funds transfer systems, EFT-based delivery systems already exist at state and local levels. Some examples are:

- New York City has had an all electronic welfare payments system in place for over three years.
- New York State has established an electronic system to

verify Medicaid eligibility.

- Ramsey County, Minnesota, is using ATMs and POS terminals to provide cash for public assistance programs.
- Reading, Pennsylvania, has established an electronic benefits system for the food stamp program.
- Washington, Arizona and New Mexico each have district pilot programs in place to provide electronic food stamps, public assistance and AFDC payments to recipients in those states.

In conclusion, for the reasons stated, EFTA strongly recommends that Congress consider an electronic funds transfer approach to deal with the government check cashing problem. These systems and technologies are already available and in use today.

We stand ready to assist the Congress in addressing this important issue.

Sincerely,

Sean Kennedy

Sean Kennedy
President and CEO

cc: Subcommittee on Consumer
& Regulatory Affairs

Senate Committee on Banking,
Housing, & Urban Affairs

STATEMENT
OF THE
CONSUMER BANKERS ASSOCIATION
BEFORE THE
SUBCOMMITTEE ON CONSUMER AFFAIRS
OF THE
BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE
UNITED STATES SENATE

June 6, 1989

Introduction

The Consumer Bankers Association* is pleased to have this opportunity to present our views on S. 906, the "Government Check Cashing Act of 1989" and S. 907, "Basic Banking Services Access Act of 1989," both authored by Senator Metzenbaum.

In fact, CBA has long been interested in the challenge of making banking services more universally accessible. Five years ago, CBA established a "Basic Banking Task Force", which was designed to explore ideas for providing such services. This work is being continued this year in the Community Development Task Force. This Task Force will look at, among other issues, direct deposit, "lifeline" or basic banking, and government check cashing.

Scope of Problem

Currently, recipients of government checks have several options for turning their funds into cash:

First, most recipients of government checks have regular checking accounts. It is important to recognize that government checks are in the normal course made payable to contractors, vendors, civilian employees, members of the military, former civilian employees, other retirees, veterans, and taxpayers entitled to tax refunds, to name just a few. The overwhelming majority of these individuals have regular checking accounts and have no need for the protection of S. 906. Indeed, according to the January 1988 issue of Consumer Reports, 80% of all adults in the U.S. have bank accounts. A study on

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* The Consumer Bankers Association was founded in 1919 to provide a progressive voice for the retail banking industry. CBA represents approximately 800 federally insured banks and thrift institutions that hold more than 80 percent of all consumer deposits, and more than 70 percent of all consumer credit held by federally insured depository institutions.

Government Check Cashing Issues completed by the General Accounting Office on October 1988 found that only 17% of the 93 million families in the United States do not have checking accounts.

Second, our information shows that a majority of the commercial banks in the country currently offer basic banking services to the public -- specially designed deposit accounts that fill basic needs at low or no cost to the consumer. The terms of these accounts vary from bank to bank on the basis of each institution's internal costs and its perception of the needs of its community. We feel it would be counterproductive to mandate that banks provide a specific type of basic banking account: since most banks already offer some type of basic banking, such legislation is not needed. In addition, outlining a specific account ignores the very different needs and capabilities of both depository institutions and customers. A small bank in a rural community should be able to tailor its basic banking account to fit its customers' needs, as should a large institution with inner city branches.

While CBA is opposed to mandatory lifeline or basic banking accounts and would like to register our opposition today, we will focus primarily on government check cashing since that issue has been the more controversial of the two. In addition to cashing checks for customers with regular or lifeline checking accounts, many of our members voluntarily cash government checks for non-customers. According to the October 1988 Government Accounting Office study, 86% of banks and 56% of thrifts in the country cashed U.S. Treasury checks for non-customers.

Finally, an option that is frequently the choice of consumers is the use of the non-depository check cashing companies that have proliferated throughout the country and are regulated by many but not all states. Possibly, part of Senator Metzenbaum's perception that a problem exists with respect to government check-cashing arises from the fact that the State of Ohio does not regulate such entities.

These businesses provide a needed service to consumers. However, the check cashing industry could be more tightly regulated than is currently the case in many states. Banks are highly regulated - the check cashing industry should be as well. In New York, check cashing is regulated by the State Department of Banking. Fees are limited to 3/4 of 1% of the face value of a check. Annually, New York check-cashers handle more than 18 million checks totalling over $5 billion. The check cashing industry is thus a significant factor in the cashing of government checks. Even if banks were required by law to cash government checks for non-customers, the check-cashing industry would still be a significant factor. We therefore feel that states should be encouraged to look closely at the state laws regulating the check cashing industry.

The city of New York has been an innovator in seeking ways to reduce losses from fraud and theft, both to banks and to the recipients of government checks. Through an electronic payment funds transfer system, in connection with a New York City bank, over 8 million welfare transactions providing over $1.6 billion of benefits are completed each year. This system reduces fraud and government costs and delivers needed services for reasonable fees. It also benefits elderly and disabled people who find it difficult to make a trip to the bank to deposit or cash a check.

Experiments patterned on the New York experience might well provide the optimal solution to any problems that exist with unregulated check-cashers.

Concerns Regarding Current Draft of S. 906

Overbreadth. The Consumer Bankers Association hopes to play a constructive role in helping to determine whether legislation is required and, if so, in fashioning legislation properly tailored to the problem at hand. Nevertheless, we must admit that we have major philosophical and practical concerns regarding S. 906 as it is currently drafted. We have hinted at some of these concerns above.

Our information indicates that approximately 8 billion government checks, constituting 20% of total check volume, are written annually. As currently drafted, government checks covered by S. 906 are limited to amounts of $1500 or less, but still include all federal, state, and local government checks below that amount. Even with the dollar limitation this amounts to billions of checks annually. The categories should be further limited in order to cut down on the potential for fraudulent checks being introduced into the system. Under the current language in S. 906, depository institutions would be required to cash all checks in the amount of $1500 or less issued by the U.S. Treasury, state governments, cities, towns and villages, public utilities, highway departments, housing authorities, hospitals, universities and colleges, and motor vehicle departments, to name a few.

The costs of processing all these checks are huge. U.S. Treasury payments alone total 700 million annually. Of these, between 500-525 million payments are made by check and the rest are direct deposit. Because the cost to Treasury of using paper checks is so high, the Treasury Department is conducting a study on the benefits of utilizing electronic payments. Treasury is also conducting a study to determine where checks are cashed. We feel that the legislation under consideration today is premature until this study is completed.

Operational problems

It costs money for a bank or savings and loan to cash a check, whether for a customer or a non-customer. A number of factors must be taken into consideration when attempting to quantify the costs to a depository institution for providing this service.

It is difficult to ascertain precisely how much it costs a given institution to cash and process a check (and costs vary from institution to institution and city to city). In computing this cost, a bank must include in its calculations all branch operating expense items, systems-related expenses, the salaries of tellers and other personnel and services such as check processing and check reconcilement. An informal survey of our members has given us a range of between $.60 and $3.50 as the estimated cost of cashing a single check, with the average cost estimate falling between $2.00 and $2.50. It is apparent from these estimates that apart from the separate and equally important issue of potential fraud losses from S. 906, the sheer operational expense of being required to cash checks for an unpredictable number of non-customers will be significant.

S. 906 would allow institutions to charge fees for this service which "do not exceed an amount needed to recover all related costs, including fraud losses, as determined by the (Federal Reserve) Board based on actual cost studies." CBA believes that the costs associated with cashing any kind of check, including government checks, are virtually impossible to quantify. Our own research, and that of the GAO was unable to come up with a figure on cost in this area. In addition, costs vary greatly and are determined by such factors as geographical location and size of an institution. Therefore CBA feels that it will be very difficult for the Fed to come up with a figure for reimbursement that will be fair to all institutions and customers.

We would also like to note that the Federal Reserve Board will soon complete a study on Regulation CC which implements the Funds Availability Act. We understand that the study will show not only that the compliance costs were very high, but also that the new statute did not appreciably change the funds availability policy of a majority of institutions. Most banks were already making funds available within the mandated schedule. New operational changes, disclosures, training requirements etc., however, necessitated expenditures, even if the bank's Funds Availability policy did not change or was slightly modified. We are concerned that enactment of S. 906 will have the same results - higher costs with no commensurate consumer benefits.

In addition to cost, S. 906 presents a number of logistical problems. Near the beginning of each month substantial numbers of non-customers would come to depository institutions in order to cash government checks. Banks and savings and loan associations will in many cases need to arrange for additional tellers and cash on hand,

and thus additional armored cars and bonded messengers. These services and costs will vary from bank to bank and city to city, depending, among other things, on the availability of competent and trustworthy part-time personnel, the ability of the institution to use "excess" personnel from other areas, the adequacy of vault space and teller stations and the number and dollar amounts of checks presented. For institutions located near military bases or other government facilities, for example, these costs will be considerable.

While some banks will be able to employ part-time personnel to service the influx of non-customer check-cashers at the beginning of each month, others will have to choose between adding full-time employees, at greater cost, or providing inadequate service. Many of CBA's institutions voiced concern that longer lines on certain days of the month and the increased volume of transactions would create a decrease in service to regular customers. This would be especially true for banks or branches located near military or other government facilities and those in low and moderate income neighborhoods. Thus, S. 906 may have the anomalous result of reducing the overall quality of service in the very areas it is designed to serve.

To illustrate the potential impact on small institutions, we would like to cite the experience of a small commercial bank in Florida which has in the past voluntarily cashed government checks for non-customers. Recently, on one day, despite having set aside 5-1/2% of its total deposit funds in its vault as a non-earning asset, it ran out of cash, and additional funds had to be transported from other institutions. Another day, 1,500 of 1,700 persons who appeared at its teller windows were non-customers cashing government checks. In other words, this increased the traffic in the bank from its daily average of 200 to 1700 people.

Likelihood of Fraud and Other Credit Losses

Fraudulent or stolen government checks are big business. Even with picture-perfect identification cards (and it is not yet clear exactly what the identification and registration procedures would be under S. 906), the prospects of massive fraud losses resulting from S. 906 loom large. A legitimate i.d. provides no protection against a stolen and altered or fraudulent check.

Provisions of the recently enacted Expedited Funds Availability Act requiring next business day crediting of government checks for customers with deposit accounts provoked a great deal of concern in the banking industry on the likelihood of fraud losses. The concern was warranted. Banks are beginning to see increases in fraud losses in this area.

Indeed, the Chairman of the Federal Reserve Board has requested Congress amend the Expedited Funds Availability Act in order to reduce this type of risk. The Federal Reserve Board's proposal would amend the Act to authorize the Board to establish regulations allowing banks

(i) to limit the amount that can be withdrawn on checks that must have next day availability, (ii) to delay the availability of funds in the event they have reasonable cause to believe that a check is uncollectible. In supporting these amendments, the Federal Reserve Board stated: "We are aware of a number of cases of this type of check fraud. Further, we believe that forgery of these types of checks would not be difficult."

These concerns are not alarmist. Even in the absence of legislation requiring check-cashing for non-customers or expedited funds availability, and despite procedures designed to minimize fraud losses, at least two of our member institutions reported losses approximating $1 million last year on fraudulent U.S. Government checks cashed for customers.

Fraud does not constitute the only credit risk in cashing government checks. Like other checks, government checks are occasionally stopped or dishonored for a variety of reasons. Under S. 906 a bank cannot wait to ascertain whether a check will clear prior to cashing it. Thus, a bank's only recourse under S. 906 would be to attempt to collect the amount from a person who does not have a customer relationship with the institution. A total loss will generally result.

Many questions remain concerning both the feasibility of and the need for mandatory cashing of government checks. As we stated earlier, last year's General Accounting Office study concluded that the vast majority of Americans have access to check cashing services. Because the size, capabilities and constituencies of depository institutions throughout the country vary greatly, it would be extremely difficult to design legislation that would effectively deal with problems related to access to check cashing services in the few areas where such problems exist.

There are alternatives to mandatory government check cashing that would be more effective in addressing this issue. Such initiatives include linking check cashing services to basic banking accounts, and working towards a wider acceptance of electronic benefits payments (direct deposit). The latter would reduce the costs to both the government agency issuing the payment and the depository institution, and would reduce fraud and theft. Elderly and handicapped individuals would certainly benefit from this step. As we stated earlier, the U.S. Treasury Department is conducting research in this area, including a pilot program in Baltimore.

Check cashing at post offices or other government offices should be evaluated. Post offices serve as an arm of the government and are located in convenient locations throughout the country. In addition, they are used to handling large amounts of cash.

Conclusions:

Because of the concerns outlined above, CBA and its members oppose S. 906 and would most likely oppose any other legislative efforts to mandate that depository institutions cash government checks for non-customers, or to mandate that they offer basic banking accounts. We believe that this is an inappropriate solution to the problem of improving access to check cashing services for the disadvantaged. As we stated earlier, the magnitude of this problem is still unclear.

We greatly appreciate the opportunity you have afforded us to offer our views on this subject.

GAO
United States
General Accounting Office
Washington, D.C. 20548

General Government Division

June 5, 1989

The Honorable Alan J. Dixon
Chairman, Subcommittee on Consumer
and Regulatory Affairs
Committee on Banking, Housing, and
Urban Affairs
United States Senate

Dear Chairman Dixon:

As you requested, a copy of our report entitled Banking: Government Check-Cashing Issues[1] is herewith submitted for inclusion in the record of your June 6 and 7, 1989, hearings on consumer banking issues. This report and earlier testimony[2] were prepared in response to the requirement in Title X of the Competitive Equality Banking Act of 1987 (Public Law 100-86) that we study and report to the Senate Committee on Banking, Housing, and Urban Affairs and to the House Committee on Banking, Finance and Urban Affairs on "the extent to which individuals who receive Treasury checks have difficulty cashing such checks."

The following briefly summarizes our results. Our study had three objectives. They were to obtain information on

- the check-cashing policies of banking institutions and nondepositor options for cashing government checks;
- the characteristics of those who do not have banking accounts and who would thus be most likely to have difficulty cashing government checks at banks; and
- governmental responses to check-cashing issues.

We found that

- Banking institutions in urban areas appear to be less likely than those in rural areas to cash nondepositor government checks. Check-cashing centers will cash them for a fee, which consumer groups often view as excessive;

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[1] GAO/GGD-89-12, October 1988.

[2] GAO/T-GGD-88-35, presented at hearings held by the Senate Banking Subcommittee on Consumer Affairs on May 18, 1988.

grocery and other stores will cash checks, although they may charge a fee or require a minimum purchase.

-- According to the latest Bureau of Census data, a majority of nondepositor families had estimated annual incomes of under $10,000, and most family heads had 12 years of education or less. Bureau of the Census data also showed that of nondepositor families receiving government checks, the three most common types of checks were Social Security, Aid to Families With Dependent Children, and Supplemental Security Income benefits.

-- Some federal, state, and local government units have taken steps to improve recipients' access to cash or other benefits and/or to lower their costs, including use of electronic funds transfer technology.

In conclusion, we recognized that there are costs associated with the cashing of government checks. If Congress determines that recipients of certain government checks should not bear these costs or should be assured of a low-cost option, we said that it should consider encouraging methods that utilize plastic cards and electronic funds transfer technology.

We also said that Congress may also wish to consider requiring the Departments of Agriculture, Health and Human Services, and Treasury, in consultation with state and local governments and banking and consumer groups, to assess the present delivery methods for all government benefits and to seek to develop coordinated delivery systems that would better meet the needs of recipients as well as reduce governmental delivery costs.

If we can be of further assistance, please call me on 275-8678.

Sincerely yours,

Craig A. Simmons

Craig A. Simmons
Director, Financial Institutions
and Markets Issues

Enclosure

United States General Accounting Office

GAO

Report to Congressional Committees

October 1988

BANKING

Government Check-Cashing Issues

GAO/GGD-89-12

GAO United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-218931

October 7, 1988

The Honorable William Proxmire
Chairman, Committee on Banking, Housing,
and Urban Affairs
United States Senate

The Honorable Fernand J. St Germain
Chairman, Committee on Banking, Finance
and Urban Affairs
House of Representatives

This report presents the results of our study of issues related to the cashing of government checks. This study responds to the requirement in Title X, Section 1001 of the Competitive Equality Banking Act of 1987.

Copies of this report are being sent to the Chairman, Board of Governors of the Federal Reserve System; the Comptroller of the Currency; the Chairman, Federal Deposit Insurance Corporation; the Chairman of the Board, National Credit Union Administration; the Chairman, Federal Home Loan Bank Board; the Secretary of the Treasury; the Secretary of Health and Human Services; the Secretary of Agriculture; and other interested parties.

Richard L Fogel

Richard L. Fogel
Assistant Comptroller General

Executive Summary

Purpose

Consumer groups and others believe that many low-and moderate-income consumers without banking accounts pay too much to have their government checks cashed. Banks and savings and loan institutions, they believe, should cash such checks for nondepositors. Banking representatives say banking institutions should not have to bear the costs of cashing nondepositors' checks.

The Competitive Equality Banking Act of 1987 required GAO to study and report on the extent to which individuals who receive Treasury checks have difficulty cashing them. GAO objectives were to obtain information on

- the check-cashing policies of banking institutions and why they resist mandatory check-cashing for nondepositors;
- the characteristics of those who do not have banking accounts—those individuals most likely to be having difficulty cashing government checks at banks; and
- governmental responses to check-cashing issues.

Background

Consumer groups have supported legislation requiring banking institutions to cash nondepositor checks for free or for a low fee. GAO could not locate any current reliable nationwide surveys that would enable policy makers to determine just how significant check cashing problems are for low- to moderate-income consumers. (See pp. 8-10.)

In agreement with the Senate Committee on Banking, Housing, and Urban Affairs and the House Committee on Banking, Finance and Urban Affairs, GAO analyzed available information on individuals' check cashing experiences and options and interviewed officials of federal bank regulatory agencies, federal program agencies, consumer and banking associations, and state and local governments. Finally, GAO analyzed a Bureau of the Census data base to determine the characteristics of recipients of government checks who do not have banking accounts. (See pp. 10-12.)

Results in Brief

GAO found that:

- Banking institutions in urban areas appear to be less likely than those in rural areas to cash nondepositor government checks. Check-cashing centers will cash them for a fee, which consumer groups often view as excessive; grocery and other stores will also cash checks, although they may charge a fee or require a minimum purchase.

- According to the latest Bureau of the Census data, a majority of nondepositor families had estimated annual incomes of under $10,000, and most family heads had 12 years of education or less. Bureau of the Census data also showed that of nondepositor families receiving government checks, the three most common types of checks were for Social Security, Aid to Families With Dependent Children, and Supplemental Security Income benefits.
- Some federal, state, and local governmental units have taken steps to improve recipients' access to cash or other benefits and/or to lower their costs, including use of electronic funds transfer technology.

GAO Findings

Access to Check Cashing

Nondepositors currently cash government checks at banking institutions, at check-cashing centers, at grocery and other stores, and through friends and relatives. They may or may not be charged a fee.

Available data suggest that banking institutions in urban areas are less likely to cash checks for nondepositors. Representatives of banking associations cite costs associated with cashing nondepositor government checks, including crowded lobbies that discourage paying customers, potential fraud, and unreimbursed expenses. While GAO was unable to obtain a definitive estimate of how much it costs a banking institution to cash a check, it does not dispute that such costs exist. (See pp. 13-18.)

Characteristics of Nondepositors

Because government check recipients who do not have an account at a banking institution are more likely to experience check-cashing problems, GAO sought to profile their characteristics. GAO's analysis of the 1985 Bureau of the Census national Survey of Income and Program Participation, the most recent data containing the needed information, showed the following:

- About 17 percent of the 92.9 million families in the United States did not have banking accounts. Fifty-six percent of these families had estimated annual incomes below $10,000, and 81 percent of the family heads had 12 years of education or less. Many nondepositor families received federal, state, and/or local government checks. The most common checks received were for Social Security benefit (3.4 million families), Aid to Families with Dependent Children (2.0 million families), and Supplemental Security Income (1.1 million families) programs. (See pp. 19-22.)

- Although Social Security beneficiaries represent the largest group of nondepositor families receiving government checks, 86 percent of all families receiving Social Security benefits had banking accounts. In contrast, only 25 percent of all families receiving Aid to Families with Dependent Children benefits and 50 percent of all families receiving Supplemental Security Income benefits had accounts. (See p. 22.)

According to consumer groups and others, the reasons why individuals do not have banking accounts include high service charges, minimum balance requirements, welfare regulations limiting beneficiaries' assets, mistrust of financial institutions, and inconvenient hours and locations of banking institutions. (See pp. 25-27.)

Governmental Responses

Some governmental entities have initiated programs and experimental projects using electronic technology to transfer benefits to recipients. At the federal level, the Social Security Administration has a new approach to encouraging direct deposit of payments to recipients' banking accounts. It is also working with the Department of the Treasury on an experiment to deliver Supplemental Security Income benefits through automatic teller machines and point-of-sale outlets. These and other efforts should help reduce check-cashing problems that some recipients of certain program benefits have experienced. (See pp. 28-39.)

Matters for the Consideration of Congress

GAO recognizes that there are costs associated with the cashing of government checks. If Congress determines that recipients of certain government checks should not bear these costs or should be assured of a low-cost option, it should consider encouraging methods that utilize plastic cards and electronic funds transfer technology.

Congress may also wish to consider requiring the Departments of Agriculture, Health and Human Services, and the Treasury, in consultation with state and local governments and banking and consumer groups, to assess the present delivery methods for all government benefits and to seek to develop coordinated delivery systems that would better meet the needs of recipients as well as reduce governmental delivery costs.

Agency Comments

Because of the nature of this report and time constraints, organizations were not asked to provide official comments.

Contents

Executive Summary 2

Chapter 1 Introduction 8
- The Use of Checks by Federal, State, and Local Governments 10
- Objective, Scope, and Methodology 10

Chapter 2 Check-Cashing Options of Families Without Banking Accounts 13
- Check-Cashing Practices of Banking Institutions 13
- Practices of Check-Cashing Centers 14
- Third Parties 15
- Why Banking Institutions Resist Cashing Checks for Nondepositors 16

Chapter 3 Characteristics of Government Benefit Recipients Who Are Nondepositors 19
- Who Is Susceptible to Check-Cashing Problems 19
- Types of Government Checks Nondepositors Receive 22
- Banking Options for Senior Citizens 23
- Comparing the Price of Low-Cost Banking Accounts and Check-Cashing Centers 25
- Why Some Families Do Not Have Banking Accounts 25

Chapter 4 Government Responses to Problems Associated With the Delivery and Cashing of Checks 28
- Federal Actions 28
- State and Local Actions 33

Chapter 5 Conclusions and Matters for Congressional Consideration 40
- Matters for Congress to Consider 41

Appendixes

Appendix I: Survey of Income and Program Participation Methodology 42
Appendix II: Number and Percent of Nondepositor Families in the United States That Receive Government Payments (1985) 44
Appendix III: Treasury Payments (FY 1987) 45
Appendix IV: Major Contributors to This Report 47

Tables

Table 2.1: Treasury Checks Reclaimed or Denied in FY 1987 17
Table III.1: Treasury Checks Issued (FY 1987) 45
Table III.2: Treasury Payments by Electronic Funds Transfer (FY 1987) 46

Figures

Figure 3.1: Estimated Yearly Income Levels of Nondepositor Families 20
Figure 3.2: Education Levels of Nondepositor Families 21
Figure 3.3: Number of Depositor and Nondepositor Families Receiving Specified Treasury Payments 23
Figure 3.4: Number of Depositor and Nondepositor Families Receiving Specified State and Local Government Payments 23

Abbreviations

CEBA	Competitive Equality Banking Act of 1987
GAO	General Accounting Office
SIPP	Survey of Income and Program Participation

Chapter 1

Introduction

In August 1987, Congress passed the Competitive Equality Banking Act of 1987 (Public Law 100-86, 101 Stat 552, August 10, 1987), which requires us to do a study and report to the Senate Committee on Banking, Housing, and Urban Affairs and the House Committee on Banking, Finance and Urban Affairs on "the extent to which individuals who receive Treasury checks have difficulty cashing such checks."[1]

Access to check-cashing services at banking institutions[2] is a difficult, complex, and emotional issue. While consumer advocacy groups and others believe that many low- and moderate-income consumers have difficulty cashing government checks, little statistically valid data exist on the extent or cause of such difficulties. Furthermore, there is disagreement as to what constitutes "difficulty."

Consumer groups have supported legislation requiring banking institutions to cash nondepositor checks for free or for a low fee. They have said that low-income individuals are often forced into costly options when cashing their checks.[3] For example, an official from the Ohio State Consumers Education Association testified in May 1988[4] that before cashing a check, many banks require welfare recipients to open accounts for fees that they cannot afford, provide drivers' licenses that many do not have for identification, and stand in separate lines. A representative of the Consumer Federation of America[5] testified at the same hearing that people may pay staggering prices when relying on check-cashing centers or other unlicensed community locations, such as liquor stores, where price gouging is the norm and personal safety is in question. She said this affects low-income people because high check-cashing costs are taken directly from their food or rent money.

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[1] The preliminary results of our study were presented in testimony by Richard L. Fogel, Assistant Comptroller General, General Government Programs (GAO/T-GGD-88-35), at hearings held by the Senate Banking Subcommittee on Consumer Affairs on May 18, 1988.

[2] In this report, the terms "banking institution" or "bank" refer to federally insured commercial banks, savings banks, and savings and loan institutions. Similarly, "banking account" refers to checking, savings, or similar accounts maintained at any of these institutions or credit unions.

[3] In March 1987, a proposed amendment to a bill, the Competitive Equality Banking Act of 1987 (CEBA), would have required depository institutions to cash nondepositor government checks free of charge. This amendment was passed by the Senate but was not included in CEBA as enacted.

[4] See testimony of Margaret Willis, Chairperson, Ohio State Consumer Education Association, before the Senate Banking Subcommittee on Consumer Affairs, May 18, 1988.

[5] A representative of the Consumer Federation of America said his organization consisted of over 230 local, state, and national consumer, senior citizen, rural, cooperative, and labor organizations that together have over 50 million members. Since 1968, it has represented these organizations before Congress and federal regulatory agencies on matters of concern to consumers. In the May hearings, it represented the American Association of Retired Persons, the Center for Community Change, the Consumers Union, the Association of Community Organizations for Reform Now, Public Citizen, and the U.S. Public Interest Research Group.

We asked federal banking regulatory agency officials if their complaint handling systems had received complaints from individuals experiencing check-cashing problems. In all cases, they said complaints had been low. For example, in 1987 the Office of the Comptroller of the Currency received 14,596 written complaints from the public of which 71, or less than 0.5 percent, dealt with check-cashing problems. Officials of the Social Security Administration, which serves about 42 million individuals, and the Veterans Administration, which serves about 4 million individuals, also said that they have not received significant numbers of check-cashing complaints.

Although these federal officials said complaints were few, we do not believe this proves that a problem does not exist. Those affected may not be sufficiently sophisticated or motivated to contact the federal regulator of the involved banking institution. This possibility is suggested by experiences in New Jersey, where one study found that 49 percent of the individuals surveyed cashing government checks at state-regulated check-cashing centers were overcharged the legal limit, but only one complaint was submitted to the appropriate state agency in 2 years.[6] Officials at the American Association of Retired Persons said that they also believe check-cashing problems exist even though they have received very few complaints about check cashing from its approximately 27 million members.[7]

On the basis of the concerns expressed primarily by consumer groups, we believe that those without banking accounts, referred to as "nondepositors" in this report, are the most likely to experience problems. However, there is little definitive data on the scope of the problems these individuals experienced. In the 1980s, several organizations did studies that focus partially on the services banking institutions and check-cashing centers[a] offer. (See ch. 2.)

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[6] A study done by the New Jersey Department of the Public Advocate reported that 322 of 662 individuals (49 percent) were charged more than the limits set by law while cashing government checks at state regulated check-cashing centers. ("Who's Checking?" An Investigation and Analysis of the Check Cashing Industry in New Jersey, the Cashing of Government-Issued Checks and the Regulatory Role of the State Department of Banking, Jan. 1988.) In her response to the study, the Commissioner of the New Jersey Department of Banking said that only one check-cashing complaint had been submitted to her department in 2 years.

[7] The American Association of Retired Persons is an organization that provides benefits, services, and privileges for its members.

The Use of Checks by Federal, State, and Local Governments

Federal, state, and local governments routinely issue checks for a multitude of purposes, including payments to vendors, contractors, employees, retirees, welfare recipients, and others. The Consumer Bankers Association[b] estimated that approximately 8 billion government checks are written annually, constituting 20 percent of total check volume.

The federal government issued 559 million Treasury checks, valued at $624 billion, in fiscal year 1987. These checks constituted 63 percent of the 890 million Treasury payments valued at about $1.2 trillion. Other Treasury payments were made using electronic funds transfer. See appendix III for additional details on Treasury payments, including checks issued.

Objective, Scope, and Methodology

The Competitive Equality Banking Act of 1987 requires GAO to study the extent to which individuals who receive Treasury checks have difficulty cashing them. Designing and carrying out a national, statistically valid survey of Treasury check recipients, however, would have been costly and would have required more time than was available. Also, because we found that banking institutions and those representing check recipients made little distinction among checks from all levels of government, the term "government checks" as used in this report refers to federal, state, and local government checks, unless otherwise noted.

As agreed with the Senate Committee on Banking, Housing, and Urban Affairs and the House Committee on Banking, Finance and Urban Affairs, the objective of our review was to examine and report on

- the check-cashing policies of banking institutions and nondepositor options for cashing government checks;

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[a] As used in this report, check-cashing centers are businesses that deal primarily in cashing checks. According to the National Check Cashers Association, Inc., these businesses operate convenient neighborhood facilities to cash checks and offer a wide variety of ancillary services to the public, including issuing money orders, providing notary public service, arranging electronic money transfers, accepting utility payments, and providing credit card cash advances.

[b] A Consumer Bankers Association official said the association represents approximately 700 federally insured banks, savings and loan institutions, and credit unions that hold more than 80 percent of all consumer deposits and more than 70 percent of all consumer credit held by federally insured depository institutions.

- the characteristics of those who do not have banking accounts—those individuals most likely to be having difficulty cashing government checks at banks; and
- government responses to check-cashing issues.

We did an extensive literature search to identify available information and analyzed relevant studies and data. We also interviewed officials of concerned or involved organizations to understand the nature of check-cashing complaints. These included national and local consumer groups, social service groups, and welfare rights groups;[10] all the federal banking institution regulatory agencies;[11] federal program agencies (Social Security and Veterans Administrations); the Department of the Treasury; and banking institution and check-cashing trade association officials.[12] We also visited state and county officials in Ohio, Illinois, and Minnesota to observe first-hand the special arrangements they have made for making benefits available. In Ohio and Illinois, we met with local consumer and banking groups as well to obtain their views. We also attended a limited number of meetings and service center events where senior citizens and welfare recipients were present. At the meetings, we asked them about their check-cashing experiences.

Because we could not locate national data on the number of individuals who believed they were having problems cashing checks, we concentrated on profiling the characteristics of government check recipients whom we were told would most likely be having problems cashing checks at banks. Using the Bureau of the Census' Survey of Income and Program Participation (1985 data that became available in 1988), we determined the number of individuals receiving checks who did not have banking accounts. This analysis enabled us to determine both the characteristics of families without banking accounts and the types of government checks they received. Additional information on our methodology is given in appendix I. We did not verify the accuracy of

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[10] Associations contacted included the Association of Community Organizations for Reform Now, the American Association of Retired Persons, and the Consumer Federation of America.

[11] The Federal Deposit Insurance Corporation, the Federal Reserve Board, the Federal Home Loan Bank Board, the Office of the Comptroller of the Currency, and the National Credit Union Administration.

[12] Associations contacted included the American Bankers Association, the Consumer Bankers Association, the National Check Cashers Association, the U.S. League of Savings Institutions, and the Independent Bankers Association of America.

Census' data; the Bureau of the Census has its own verification procedures. In addition, we also reviewed data from Federal Reserve-sponsored surveys regarding the characteristics of families without banking accounts.

There is no single definitive source for the volume and dollar values of Treasury payments by program. To develop such estimates, we worked closely with officials of the Treasury's Financial Management Service. This office maintains volume data and aggregate dollar value data. We also contacted appropriate federal program agencies to obtain data on the dollar values by program. Congressional offices have asked us to include this data in our report. The specific Treasury reports used are cited in appendix III, table III.1. We also obtained information on reclamation and declination[13] of Treasury checks from the Financial Management Service in order to determine fraud levels. Our work was done in accordance with generally accepted government auditing standards.

Because of the nature of this report and time constraints, organizations were not asked to provide official comments. Instead, their officials were given an opportunity to provide comments either on our May 1988 testimony on this subject or on the matters dealing specifically with their organizations. Any comments received have been incorporated and attributed as appropriate. Such input was sought from the federal banking regulators, the Social Security Administration, the Veterans Administration, the Department of Treasury, banking trade associations, and the Consumer Federation of America.

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[13] Reclamation is when Treasury reclaims money from financial institutions that cash Treasury checks with forged or unauthorized endorsements. Declination is when Treasury refuses payment on Treasury checks that have been materially changed, such as on altered or counterfeit checks.

Check-Cashing Options of Families Without Banking Accounts

There is no single definitive nationwide or regional study of current check-cashing practices of banking or other institutions. Our analysis of the available data suggests, however, that banking institutions in rural areas are more likely than those in urban areas to cash nondepositors' government checks. Other check-cashing options for nondepositors include check-cashing centers, which are located in most states and whose check-cashing fees are regulated in several states; relatives or friends; and grocery and other stores. All of these options may involve fees or, in the case of stores, a minimum purchase.

Check-Cashing Practices of Banking Institutions

We made a nationwide statistically valid survey of fees charged by banks and thrifts for banking accounts and other services.[1] We found that as of mid-1985, about 86 percent of banks and 55 percent of thrifts cashed U.S. Treasury checks for nondepositors. Of that total, nearly 56 percent of banks and 84 percent of thrifts cashed Treasury checks free of charge. For those that charged for the service, the median fee was about $2.00.

In surveying one-quarter of its membership (1,767 banks) in 1984, the Independent Bankers Association of America found that 68 percent of the responding banks cashed nondepositors' government checks free of charge. According to an association official, this percentage was high because most member banks are locally owned and operated in small towns or rural areas. While only approximately one-third of the surveyed banks responded to the questionnaire, the official told us he believes most of the banks affiliated with his association cash checks free of charge for nondepositors.

Surveys made by consumer groups reveal different, though not necessarily contradictory, results from those obtained by us and the Independent Bankers Association of America. According to a study by the Association of Community Organizations for Reform Now, 12 percent of 344 financial institutions surveyed cashed government checks for nondepositors in 1986.[2] A 1988 Consumer Federation of America survey found that of 191 financial institutions, located primarily in urban areas, some 29 percent cashed government checks for nondepositors.[3]

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[1] Banking Services: Changes in Fees and Deposit Account Interest Rates Since Deregulation (GAO/GGD-87-70, July 1987).

[2] Bankers Lock-Out Poor People (Apr. 17, 1986).

[3] Bank Fees on Consumer Accounts, The Fifth Annual National Survey (June 8, 1988).

This study also showed that 86 percent of the financial institutions offering check-cashing services for nondepositors charged a fee, which averaged $3.88 for a $300 government check. Consumer Federation of America surveys done in 1986 and 1987 reported similar results.

Our study was the only one that was based on random sampling that could be projected nationwide. The surveys done by the Independent Bankers Association of America, the Association of Community Organizations for Reform Now, and the Consumer Federation of America, on the other hand, were not based on such sampling of all banking institutions and cannot be projected to the overall banking industry.

There are other differences in the surveys. Information in our survey was obtained from responsible officials at bank headquarters and probably reflects overall institution policies. However, branch practices may vary because of local circumstances. The studies done by the Association of Community Organizations for Reform Now and the Consumer Federation of America, on the other hand, were made at the branch level, and the results may not represent the institutions' overall policies.

On the basis of these studies, it seems reasonable to conclude that banking institutions in urban areas are less likely to cash checks for nondepositors than are banks in rural areas. The limited number of officials we spoke to about this agreed, including representatives of a consumer group and the banking industry and officials of federal banking institution regulatory agencies.

Practices of Check-Cashing Centers

Check-cashing centers are one alternative for those who do not want to or cannot cash checks at banking institutions. According to the National Check Cashers Association, which was formed in 1987, about 3,000 outlets operate in 46 states and the District of Columbia, mostly in urban areas. Other information corroborates this urban concentration. For example, a 1986 annual report of the Illinois Department of Financial Institutions reported that 519 (97 percent) of the 537 check-cashing centers that were open to the general public in Illinois were located in the greater Chicago area.

Check-cashing center check-cashing practices, although regulated in several states, are largely unregulated in the United States. The regulated maximum fees for Illinois, New York, and New Jersey are respectively:

- Illinois: 1.2 percent of the face value of the check, plus 90 cents;

- New York: 0.75 percent of the face value of the check, plus 10 cents; and
- New Jersey: 1 percent of the face value of the check for in-state checks, and 1.5 percent for out-of-state checks, up to a maximum of $8.00.

In these states, the regulated maximum fee for cashing a $411.45 check (the average amount of a Social Security benefit check in November 1987) varied from $3.19 in New York to $6.17 in New Jersey.[4] The fee in New Jersey is 1.5 percent because a Social Security check is considered an out-of-state check.

In 1987, the Consumer Federation of America did a telephone survey of fees charged by 60 check-cashing centers in 20 major cities located in 16 states and the District of Columbia.[5] The study found that check cashers usually charged a percentage of the amount of the check and that this percentage depended in part upon the type of check being cashed. For example, a distinction was made between a payroll and a personal check. The study did not find any differences between the fees charged to cash federal, state, or local government checks. Charges to cash a $500 government check ranged from 0.75 percent plus 10 cents ($3.85) in New York City, New York, to 5 percent ($25) in Los Angeles, California. (As noted earlier, New York is one of the states that regulate check-cashing fees.) The median charge was 1.5 percent ($7.50), and the average was 1.69 percent ($8.47). Since the states, cities, and check-cashing centers in this survey were not selected randomly, the survey results cannot be viewed as a statistically valid representation of nationwide practices.

Third Parties

Grocery and other stores also cash checks for individuals. In some instances, a fee is charged or a minimum purchase is required in lieu of a fee. Individuals may also endorse their checks over to friends or family members who can cash them. We have identified no national data on check-cashing activities of such third parties.

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[4] Regulations governing check-cashing fees may not always be enforced, however. A 1987 study by the New Jersey Department of the Public Advocate reported that 26 of 29 check-cashing centers surveyed were overcharging public aid recipients. Collectively, these 26 check-cashing centers overcharged approximately one-half (322) of the 662 recipients who responded to the department's questions. The reported average overcharge was $.75 per check and the range of overcharges was between $.01 and $21.25. The department also telephoned 77 New Jersey licensed check-cashing centers to obtain fee information directly. Of the 62 that gave out such information, 14 quoted a fee exceeding the regulated rate. Of the 48 that quoted a permissible fee, 18 were identified in the on-site interviews described above or in complaint letters as overcharging customers. (See "Who's Checking?")

[5] National Survey of Check Cashing Outlets (Sept. 1987).

Why Banking Institutions Resist Cashing Checks for Nondepositors

Representatives of banking associations have said they oppose legislatively mandated free check cashing for nondepositors because banking institutions would (1) not be reimbursed for costs, (2) experience congestion in their lobbies and facilities from nondepositors, and (3) incur an increased risk of fraud for which they would not be compensated.[6]

Unreimbursed Cost

Representatives of banking associations told us and have testified before Congress that banks should not be required to cash checks without compensation because of what it costs them to provide this service. They were, however, unable to give us definitive estimates of how much it costs to cash a nondepositor's government check. Check cashing involves many indirect costs, the amount of which may depend on the location and size of a bank and other factors. We were told some of the most common costs include providing additional tellers on certain days, transporting and securing extra cash, and lost interest income.[7] Several banking industry officials believe that if free check-cashing for nondepositors were legislatively mandated, the costs to the banks, if excessive, could result in some marginally profitable bank branches in low-income areas being closed. We obtained a range of check-cashing cost estimates. The Federal Reserve Board's 1987 Functional Cost Analysis survey found that the cost of processing a check ranged from 33.4 cents for a bank with deposits under $50 million to 37.7 cents for a bank with deposits over $200 million. (A Federal Reserve Board staff official emphasized to us that these figures do not capture all the costs involved in cashing checks.) A bank official estimated the cost of cashing a check at 66 cents per check for his little bank in Florida.[8] A bank in Ohio charged $2.00 to cash nondepositors' government checks, a fee that it believed basically covered its costs.

Crowded Lobbies

Representatives of banking associations said that the presence of large numbers of individuals in banking institution lobbies the few days a month when government checks are received strains both labor and resources, resulting in poor service to both the recipients of government checks and the institution's regular paying customers. For example, the small bank in Florida said that on one day at the start of a month it served approximately 1,700 people, 1,500 of whom were nondepositors cashing government checks. A spokesman for a consumer advocacy group countered that if more banks cashed nondepositors' checks, congestion problems at individual banks would be less severe.

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[6] See the May 18, 1988, statements of Alan Heuer on behalf of the Consumer Bankers Association and August Zinsser, III on behalf of the American Bankers Association before the Senate Banking Subcommittee on Consumer Affairs.

[7] Lost interest income is the earnings lost when funds are kept readily available to cash checks rather than invested.

[8] According to the bank official, this figure does not include all costs, such as costs for supervision or approving the checks, losses from bad checks or returned items, office supplies, maintenance on equipment, and janitorial services.

Potential Fraud

Representatives of banking institutions said that federal legislation requiring banks to cash government checks for nondepositors may increase the already present risk of fraud. They fear that banks would have to cash checks even if they suspected the checks were fraudulent, that the development of a reliable identification system is not feasible, and that the probability of fraud will be increased simply because the number of checks banking institutions cash will increase.[9]

We have been unable to determine the amount of money banks lose because government checks are fraudulently cashed. However, as shown in table 2.1, the actual amount Treasury reclaimed from banking institutions or refused payment on in fiscal year 1987 amounted to 10 cents for every $1,000 of checks issued, or 3 checks out of every 10,000 issued. (The aggregate data do not reflect regional and local differences.) These checks were cashed or deposited by account holders as well as nonaccount holders.

Table 2.1: Treasury Checks Reclaimed or Denied in FY 1987

	Issued	Reclaimed or denied payment[a]	Percent
Volume	558.9 million	142,632	0.03%
Value	$623.9 billion	$63.7 million	0.01%

[a] These statistics represent collections on checks due to reclamations and denials.

Source: U.S. Department of the Treasury.

These figures do not accurately reflect ultimate banking institution losses from Treasury reclamations or denials (declinations) because banks are able to collect some of the amounts reclaimed or denied from the individuals or businesses who cashed the checks. Banks and their representative organizations were unable to provide data on the extent to which they are able to collect in these instances and at what cost. Their officials told us that banks have the least difficulty recovering funds from those with banking accounts. For example, in the case of deceased payees, funds may have been building up in the payee's account after his or her death. Of the 142,632 checks collected on in fiscal year 1987, about 92,000, or 65 percent (valued at $38.9 million), were issued to deceased payees. According to Financial Management Service and U.S. Secret Service officials in Treasury, a spouse or relative usually cashes the check or deposits it in an account, in many cases believing he or she is entitled to it.[10]

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[9] Several bankers said that a unique problem with Treasury checks has been that the Treasury could reclaim checks up to 7 years after they were cashed, making it very difficult for the bank to locate the responsible party and recover the funds. This problem should be eased somewhat by Title X of the Competitive Equality Banking Act of 1987 (31 U.S.C.§ 3328), which reduces the allowed recovery time to 1 year and is scheduled to take effect on October 1, 1989, or at such time as designated by the Secretary of the Treasury.

According to the U.S. Postal Service, in fiscal year 1987, 80,024 checks were stolen from the mail and later negotiated. About equal numbers of federal and state checks were involved, which together accounted for about 95 percent of the stolen checks. Post Office officials said the checks stolen with the greatest frequency were those delivered on a regularly scheduled day, such as Social Security and Supplemental Security Income checks.

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[10] The Secret Service investigates the illegal cashing of Treasury checks. In fiscal year 1987, Treasury reported forwarding 64,844 checks for investigation to determine whether the payee benefited from the cashed check and whether fraud or forgery had taken place.

Chapter 3

Characteristics of Government Benefit Recipients Who Are Nondepositors

According to the latest available Census data, a majority of nondepositor families[1] have estimated annual incomes below $10,000, and most family heads have 12 years of education or less. The latest available data from the Bureau of the Census also shows that the three most common government checks that nondepositor families receive were for Social Security, Aid to Families with Dependent Children, and Supplemental Security Income benefits. While only 25 percent of all families receiving Aid to Families with Dependent Children and 50 percent receiving Supplemental Security Income have banking accounts, 86 percent of all families receiving Social Security benefits had banking accounts.

Consumer groups and others cite many reasons as to why individuals do not have banking accounts, including high service charges, minimum balance requirements, welfare regulations limiting beneficiaries' assets, mistrust of financial institutions, and inconvenient hours and locations of banking institutions.

Who Is Susceptible to Check-Cashing Problems

Banking, government, and consumer group officials whom we spoke with generally agreed that low-income individuals without banking accounts are likely to have check-cashing problems at banks. We analyzed the Bureau of the Census' Survey of Income and Program Participation data to determine the characteristics of those without banking accounts. Appendix I describes this nationally projectable survey, which includes information on banking account ownership; family characteristics; and receipt of federal, state, and local government monetary and other benefits. It also describes our analysis methodology.

Our analysis of 1985 Bureau of the Census data, which is the most recent census data available with the needed information, shows that about 17 percent of 92.9 million families in the United States did not have banking accounts. As shown in figures 3.1 and 3.2, over half of these families had incomes below $10,000 and the family heads had 12 years of education or less.

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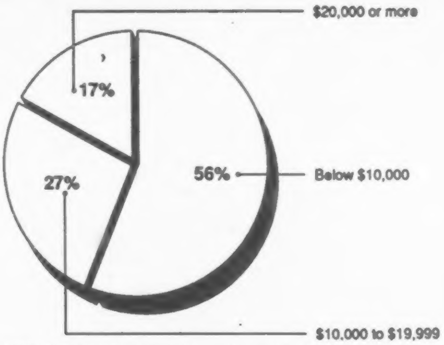
[1] As used in this report, the word "family" refers to a group of individuals who share a household and are related by blood, marriage, or adoption.

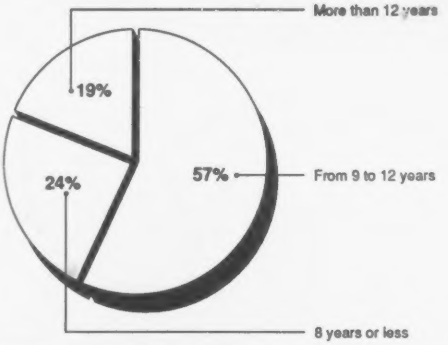
Figure 3.1: Estimated Yearly Income Levels of Nondepositor Families



Note: We obtained the estimated annual income by multiplying family income during the month of August 1985 by 12. The standard error for all figures is less than plus or minus 1 percent.

Source: Bureau of the Census, Survey of Income and Program Participation, 1985 data, as analyzed by GAO.

Figure 3.2: Education Levels of Nondepositor Families



Note: The standard error for all figures is less than plus or minus 1 percent. Figures have been rounded to ensure that the total is 100 percent.

Source: Bureau of the Census, Survey of Income and Program Participation, 1985 data, as analyzed by GAO.

The Federal Reserve-sponsored surveys examining banking account usage in 1977, 1983, 1984, and 1986[2] also sought to determine the number of families that did not have banking accounts. According to this survey data, the proportion of nondepositor families remained fairly constant, fluctuating between 8 and 12 percent for these years.[3] In some Federal Reserve publications and one draft memorandum based on these data, staff describe nondepositor families as predominantly low-income (incomes under $10,000), nonwhite, and headed by individuals with 12 years of education or less.[4] The Federal Reserve staff attribute any decline in checking account ownership over these years to an increase in the number of low-income, nonwhite, less educated families headed by single females. They believe this group is less likely to have checking accounts.[5]

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[2] These surveys were used in the following Federal Reserve Bulletin articles: (1) "Survey of Consumer Finances, 1983," (Sept. 1984); (2) "Basic Banking," (Apr. 1987); (3) "The Use of Cash and Transaction Accounts by American Families," (Feb. 1986); and (4) "Changes in the Use of Transaction Account and Cash from 1984 to 1986," (Mar. 1987). They were also used in other Federal Reserve publications, including (1) "Bank Service Charges and Fees: Their Impact on Consumers, 1984;" and (2) "Additional Evidence on Deposit Account Ownership: Changes and Usage Factors," a 1986 draft memorandum from the Federal Reserve Board's Division of Research and Statistics.

[3] According to a Federal Reserve official, the percentage of families that did not have banking accounts was 9 percent in 1977; 12 percent in 1983; 8 percent in 1984; and 10 percent in 1986. The corresponding sampling errors were 1.6 percent in 1977; 1.5 percent estimated in 1983; 1.7 percent in 1984; and 2.6 percent in 1986.

Types of Government Checks Nondepositors Receive

The Bureau of Census data show that many nondepositor families receive Treasury, state, and/or local government benefit checks. A larger proportion of nondepositor families received state and local government benefit checks than Treasury checks. (See figs. 3.3 and 3.4.)

In 1985, the most common government check nondepositor families received was Social Security; 3.4 million out of 15.7 million nondepositor families received them. Aid to Families with Dependent Children checks were received by 2 million families and Supplemental Security Income by 1.1 million families. Although Social Security recipients represent the largest group of nondepositor families that receive government checks, 86 percent of all families receiving Social Security benefits had banking accounts. In contrast, only 25 percent of all families receiving Aid to Families with Dependent Children benefits and 50 percent of all families receiving Supplemental Security Income benefits had accounts.

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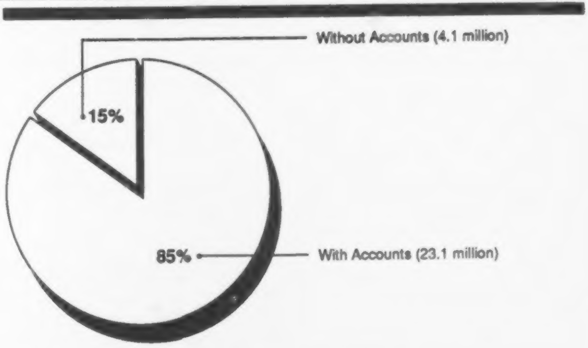
[4] The 1983 survey further segmented nondepositor families between those with 12 years of education and those without 12 years of education. This survey showed that the percentage of families with 12 years of education who had banking accounts was about the same as those with more than 12 years of education.

[5] Our analysis of the Bureau of the Census data, which has a standard error of less than plus or minus 1 percent, shows that 17 percent of all U.S. families did not have banking accounts in 1986. (See p. 19.) According to a Federal Reserve official, the survey estimates were 8 percent in 1984 and 10 percent in 1986, with sampling errors of 1.7 and 2.6 respectively. The disparities cannot be fully reconciled, but a Federal Reserve official told us they can be explained, at least in part, by the different types of surveys, sample sizes, and the definition of family. The Federal Reserve-sponsored surveys were telephone surveys of 1,946 randomly selected "families" (defined as households) in 1984 and 668 in 1986. The Bureau of the Census sample, on the other hand, involved random selection and personal interviews of adults in 14,902 households. Because the Federal Reserve-sponsored surveys were made by telephone and some low-income families may not have telephones, they may have sampled low-income families less frequently than their proportion to the total population. Because the majority of families without banking accounts have low incomes, the estimate of nondepositor families may thus be too low. Another reason for the differences is that the surveys define "family" differently. The Federal Reserve-sponsored surveys define family as all individuals living in a household; but, the Bureau of the Census definition is all individuals in a household related by blood, marriage, or adoption. As a result, the Bureau of the Census classified some households as two or more families, while the Federal Reserve sponsored surveys considered them as one.

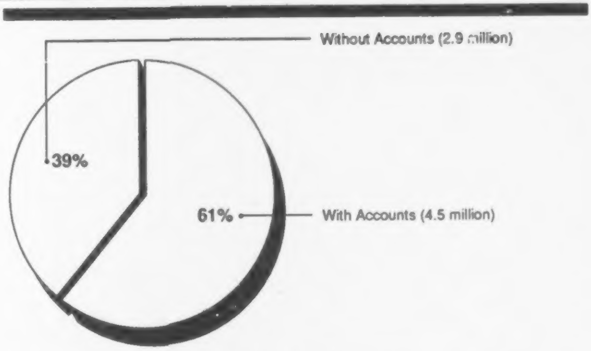
Figure 3.3: Number of Depositor and Nondepositor Families Receiving Specified Treasury Payments



Note: The standard error this data is less than plus or minus 1 percent

Source: Bureau of the Census, Survey of Income and Program Participation, 1985 data, as analyzed by GAO.

Figure 3.4: Number of Depositor and Nondepositor Families Receiving Specified State and Local Government Payments



Note: The standard error for this data is less than plus or minus 1 percent

Source: Bureau of the Census, Survey of Income and Program Participation, 1985 data, as analyzed by GAO

Low income was a consistent characteristic of families without accounts that received Social Security, Aid to Families with Dependent Children, and Supplemental Security Income benefits. Sixty-nine percent of nondepositor families receiving Social Security checks had estimated 1985 incomes below $10,000; 80 percent of nondepositor families receiving Aid to Families with Dependent Children had estimated incomes below $10,000; and 79 percent of nondepositor families receiving Supplemental Security Income had estimated incomes below $10,000.[6] Appendix II shows the number of recipient families of these major government benefit and other programs and the percentage, by program, of those who do not have banking accounts.

Banking Options for Senior Citizens

Senior citizens who receive Social Security or other benefits may find it more advantageous to have banking accounts than others because (1) the Social Security Administration is attempting to make enrollment in its direct deposit program as easy as possible for Social Security and Supplemental Security Income beneficiaries and (2) banks are more willing to offer attractive low-cost accounts to senior citizens than to the general public.

In May 1988, the Social Security Administration changed its procedures for registering new beneficiaries in an effort to increase the number of directly deposited benefits. When new recipients apply for Social Security retirement benefits, the agency assumes that if the beneficiaries have accounts at banking institutions they will receive their funds via direct deposit unless they specifically request otherwise. Before this policy, the agency assumed new beneficiaries would initially receive their checks in the mail and perhaps arrange with their banks to have them directly deposited at a later date. Through the new program, the agency hopes that the number of direct deposit beneficiaries will increase from about 45 percent in 1987 to 60 percent by 1990.

Our earlier survey found that 76 percent of banking institutions provided or planned to provide special discounted checking accounts to senior citizens but only 18 percent provided or planned to provide such accounts to the general public.[7] In December 1987, we spoke to over 100 senior citizens who were present at a senior service center we visited in San Francisco, California. Most were Social Security recipients. We found no one who claimed to be having problems cashing checks. The supportive services coordinator, who provides financial counseling for the center's approximately 2,500 clients, said she was not aware of any clients having check-cashing problems.

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[6] The standard error for all figures in this paragraph is less than plus or minus 1 percent.

[7] Banking Services, p. 60.

Comparing the Price of Low-Cost Banking Accounts and Check-Cashing Centers

The available data, which is not representative nationwide, suggest that maintaining a low-cost banking account is less expensive than using many check-cashing centers. However, this may not be consistently the case nationwide because both the fees for check-cashing centers and the availability of low-cost accounts vary considerably.

In our earlier report on banking fees and services, we calculated the price of "no frills" checking accounts for consumers who had incomes under $10,000, wrote eight checks per month, and maintained an approximate balance of $260.[8] We reported that 37 percent of these consumers would be able to have a free account, 33 percent would pay between $1.00 and $3.99 per month, and 17 percent would pay $4.00 or more per month. (We could not determine the cost for the remaining 13 percent of the consumers.)

Check-cashing center fees may exceed these monthly checking account charges. For example, the Consumer Federation of America found that, on average, check cashers charged $8.47 to cash one $500 government check. Even in New York, New Jersey, and Illinois, where check-cashing center fees are regulated, cashing one $500 government check costs between $3.85 and $7.50. The Consumer Federation of America has concluded that consumers would generally pay less at banking institutions than at check-cashing centers and would get more for their money.[9]

Why Some Families Do Not Have Banking Accounts

No definitive information exists on why some families do not have banking accounts. Some consumer groups believe, however, that the cost of banking accounts has priced many low-income families out of the market. According to our previous survey, only 18 percent of banking institutions in mid-1985 offered or planned to offer low-cost checking accounts to the general public. Furthermore, some of these may have been inappropriate for low-income individuals. For example, some had minimum balance requirements that could be prohibitive for low-income individuals.

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[8] Banking Services, p. 62.

[9] National Survey of Check Cashing Outlets, Consumers Federation of America (Sept. 1987).

Individuals who work with welfare recipients told us that some of these beneficiaries may choose to remain outside the banking system because of the asset limits contained in welfare statutes. For example, federal regulations do not permit Aid to Families with Dependent Children benefits for families with more than $1,000 in certain types of real and personal property, including cash, savings, and checking accounts. State regulations can lower this ceiling even more.

Other reasons mentioned for not having banking accounts include mistrust of banking institutions, lack of mathematical and reading skills, lack of enough money or transactions to justify an account, inconvenient bank hours and locations, delayed access to funds, requirements to open an account that include identification with a major credit card, and a lack of bilingual materials and personnel.

No nationwide data has been compiled that quantifies where nondepositors cash their checks. Several individuals and organizations we spoke with, however, said that many do not use banks. For example, National Check Cashers Association officials said many of that industry's customers are low-income individuals who do not want or cannot afford a banking account.

On three different dates, the New Jersey Department of the Public Advocate asked a total of 750 individuals outside 29 check-cashing centers why they did not cash their checks at banks. Approximately 50 percent of the 1,072 responses indicated that banks were inconvenient. Inconveniences cited included long lines at those few banks that did cash checks for nondepositors, receipt of checks on days when banks were closed, and inability to both cash checks and obtain food stamps at the same location. Other responses given for not going to banks included not having an account (20 percent), bank refusals to cash nondepositors' checks (19.5 percent), and a lack of nearby banks (8.6 percent).

The New Jersey Department of the Public Advocate also examined 4,842 cancelled Aid to Families with Dependent Children checks from December 1986 and February 1987 caseloads in three counties. They found that 53 percent of these checks were not cashed at conventional banking institutions. Some 32 percent were cashed at state licensed check cashers and 12 percent were cashed at 179 unlicensed community locations, such as neighborhood grocery stores, supermarkets, drug stores, department stores, liquor stores, bars, furniture stores, beauty shops, bowling alleys, and funeral parlors. Nine percent were cashed by friends, relatives, or landlords.

About 47 percent of the checks were cashed at banking institutions. Over three-quarters of these checks were cashed at banks serving as depositories for county Aid to Families with Dependent Children or administrative funds. Because of contractual agreements with the county, these banks were obligated to cash checks for recipients of Aid to Families with Dependent Children, regardless of whether or not they were depositors.[10]

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[10] "Who's Checking?"

Chapter 4

Government Responses to Problems Associated With the Delivery and Cashing of Checks

Federal, state, and local governments have acted to improve the delivery of payments, including lowering their administrative costs and/or assisting recipients to obtain benefits. These actions include encouraging institutions to provide basic banking services and increasing their use of electronic technology to provide benefits more economically and conveniently. While these initiatives have helped reduce check-cashing problems for some, they have been implemented on a limited basis.

Federal Actions

In the mid-1980s, federal bank regulators developed and issued policy statements urging banking institutions to voluntarily provide low-cost basic banking services to consumers, including low- and moderate-income, young, and retired persons.

Federal agencies have also been using electronic funds transfer technology for over a decade to more effectively and efficiently distribute salaries and benefits directly to the banking accounts of recipients who select this option. The Vice Chairman of the Federal Reserve Board has recently testified that the Board believes electronic alternatives represent a much better long-term solution to check-cashing problems than does a requirement that banks cash nondepositors' checks.[1] The Office of Technology Assessment has reported that federally funded assistance programs will inevitably move to some form of electronic delivery system within the next 5 to 15 years.[2]

Demonstration projects using electronic funds transfer but not requiring recipients to have banking accounts are currently being developed or are under way for a limited number of participants in certain benefit programs administered by the Department of Agriculture and the Social Security Administration.

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[1] Statement by Manual H. Johnson before the Senate Committee on Banking, Housing, and Urban Affairs (Sept. 8, 1988).

[2] The report also says that key policy issues that need to be addressed are: selecting the best technology option to follow, resolving privacy and security implications, and assessing the programmatic effects of changing to electronic systems. Electronic Delivery of Public Assistance Benefits: Technology Options and Policy Issues: Background Paper (OTA-BP-CIT-47, Apr. 1988).

Policies Were Established by Federal Bank Regulators, but Compliance Is Unknown

In 1985, the Office of the Comptroller of the Currency issued a banking circular entitled Basic Banking Services.[1] It encouraged national banks to voluntarily provide basic banking services to customers, including the young, the retired, and those with low- and moderate-incomes. Officials said the statement was the result of repeated complaints about check-cashing problems heard at meetings sponsored by the Office in 1985 and 1986. The policy statement was not mandatory, they said, because no hard evidence was provided that people were having major problems.

In 1986, the Federal Financial Institutions Examination Council[2] adopted a "Joint Policy Statement on Basic Financial Services" that was similar to the circular developed by the Office of the Comptroller of the Currency. It too was voluntary, differing primarily in that it called on bank trade associations to encourage and monitor compliance by their member banks. A council official said that compliance was anticipated through "moral persuasion" and that the council did not want the policy to become a regulated aspect of banking activities. The policy did not, however, provide clear criteria defining basic or low cost banking.

In April 1987, the Office of the Comptroller of the Currency directed its examiners to monitor national bank compliance with the policy statement during compliance examinations of these banks. (Such exams assess bank compliance with various laws and regulations.) Officials said the examiners were to look for the availability of basic banking services, including the free cashing of government checks. Considering the examination schedules for national banks, the results will not be known until 1989 for all of the large banks and at an unknown later time for smaller banks. An official at the Federal Deposit Insurance Corporation said that in 1988, questions dealing with implementation of the policy statement were approved and provided to its bank examiners for their use during compliance examinations of banks the corporation supervises—federally insured state-chartered banks that are not members of the Federal Reserve System. Officials at both regulatory agencies, recognizing that compliance is voluntary, said that they want to be aware of the level of bank acceptance and implementation of the policy statement. (The results, we believe, may be of limited value because neither agency provided clear criteria defining basic or low-cost banking.)

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[1] Banking Circular No. 206 (Aug. 23, 1985).

[2] Members of the council include the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, the Federal Reserve System, the Office of the Comptroller of the Currency, and the National Credit Union Administration.

Federal Use of Direct Delivery Is Being Expanded

Since the 1970s, the Department of the Treasury has worked with various federal agencies to promote electronic distribution of wages and other monetary benefits.[5] Payments are sent electronically to banking institutions, which credit the recipients' accounts. Appendix III shows the number of payments made using electronic funds transfer technology during fiscal year 1987. In the 1980s, experiments with automated electronic systems have also been developed to distribute noncash benefits, such as food stamps. This technology may eventually permit the use of a single distribution system to dispense cash and noncash benefits.

Electronic funds transfer offers significant cost savings to the federal government. Treasury officials estimate that as of July 1988, the cost of preparing and mailing an individual check was 30 cents. In contrast, the cost of making an electronic funds transfer payment was 4 cents.[6]

Automated Delivery of Benefits by the Social Security Administration

Public Law 92-366 (31 U.S.C. 3332), enacted August 7, 1972, authorized the federal government to make federal benefit payments directly to banking institutions at the request of the beneficiary. Shortly thereafter, the Department of the Treasury and the Social Security Administration began studying how to implement a comprehensive direct deposit program; in 1974 they agreed to provide for direct deposit of recurring Social Security payments. By March 1979, about 25 percent of these beneficiaries had elected this option. Periodic information flyers were placed in the check envelopes to inform new beneficiaries of the direct delivery option, and for about the past 10 years the rate of growth has been about 2 percent annually. As of May 31, 1988, about 47.5 percent of Social Security beneficiaries had chosen this method of payment.

The Social Security Administration believes direct deposit is a safe and convenient way for beneficiaries to receive their payments. Because electronic delivery to beneficiaries' banking accounts is more reliable than mailing checks to the beneficiaries, direct deposit also helps reduce field office workloads. According to Treasury officials, there is one allegation of nonreceipt for every 1,087 checks issued but only one allegation of nonreceipt for every 8,794 direct delivery payments made. When problems do occur, they are usually resolved in a few days, but problems with checks can take months to resolve.

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[5] A very small number of banking institutions do not have the capability to receive electronic fund transfer wire transfers. Recipients with accounts at such institutions can still receive the benefits of direct deposit by having the federal government mail their checks directly to the institution.

[6] The full use of electronic funds transfer would not translate into a potential savings for all the payments currently made by check because some checks are mailed in bulk at lower cost, and also because not all payments can be made using electronic funds transfer.

In May 1988, the Social Security Administration and the Department of the Treasury introduced a program that is expected to significantly increase the use of electronic funds transfer by Social Security beneficiaries. Under this program, direct deposit actions can be taken based on a phone call by beneficiaries already receiving benefits, and Social Security offices will presume that new beneficiaries with banking accounts will receive their benefits through direct deposit. This replaces the former policy of presuming new beneficiaries will receive checks and might convert to direct deposit in the future. Social Security Administration officials estimate that by 1990 at least 60 percent of all Social Security benefit recipients will receive payments electronically. This program is applicable only to beneficiaries with banking accounts or those who are willing to open banking accounts.

Department of Agriculture's Automated Food Stamp Delivery Project

Since the early 1980s, the Department of Agriculture's Food and Nutrition Service has been experimenting with various ways to improve the efficiency and integrity of benefit issuance in the Food Stamp Program. A major effort has been a project, initiated in July 1983, to develop and demonstrate an automated system for the issuance and redemption of food stamp benefits. This federally supported project, which took place in Reading, Pennsylvania, between October 1984 and December 1985, served an average food stamp caseload of about 3,400 households. Those households made over 25,000 electronic food purchases in about 125 retail food stores each month. When the initial demonstration project ended, the Pennsylvania Department of Public Welfare assumed responsibility for extended demonstration project operations.

When certified eligible for benefits, food stamp recipients received a magnetic striped plastic card, training on how to use it, and a secret identification number. Benefits were electronically deposited in each household account, and the recipient then used the card to buy food at any store participating in the program. The check-out counters of stores were equipped with electronic point-of-sale terminals that accessed the recipient's account once the card and secret identification number were entered. After the cashier entered the amount of the purchase, the computer checked the recipient's account, debited it, credited the retailer's account, and printed out a receipt for the recipient that showed the purchase amount and the remaining balance.

The October 1984 to December 1985 program was assessed under a contract issued by the Department of Agriculture. The resulting report said that the system was operationally feasible and, except for cost, was well received by the various parties involved in its use. While electronic-benefit-transfer costs exceeded costs for a food stamp coupon system by a ratio of about 9 to 1, this was attributed primarily to a combination of high operating costs resulting from the use of dedicated staff and equipment and a small average demonstration caseload of about 3,400 households. The report noted that the operating costs could be substantially reduced. It also said that about 77 percent of the surveyed recipients preferred the new system. In contrast, only 17 percent preferred coupons. Groups that were expected to have difficulty with the new system also strongly favored it, including the elderly, handicapped, non-English speakers, and those with little education. In no demographic group did fewer than 70 percent prefer the system. The reasons recipients said they preferred the new system included ease of use and less time and costs required to obtain and use their benefits.

The department advised the state on how the administration of the program could be integrated with other state welfare programs, such as Aid to Families with Dependent Children and General Assistance. This integration involved a transfer of the system to existing state equipment, with technical enhancements being designed to improve service to recipients and retailers. A Department of Agriculture official said that costs have been reduced, but integration has been difficult. A report on the program's progress was scheduled to be available in the fall of 1988.

In September 1987, the Department of Agriculture announced plans for additional demonstration projects emphasizing cost effectiveness. The number of sites chosen will depend on the quality of the proposals and their costs. Thirteen concept papers were received, and nine sites were invited to submit applications. About $1.8 million is available for the projects. The department wants the project sites to be ready to begin operations no later than September 30, 1989. To reduce costs, participating state and local agencies will be permitted to integrate other government programs, such as General Assistance and Aid to Families with Dependent Children.

Distribution of Supplemental Security Income Benefits

The Department of the Treasury and the Social Security Administration are planning to test the electronic disbursement of Supplemental Security Income payments using automatic teller machines and point-of-sale outlets. The test initiative will target Supplemental Security Income recipients because only about 14 percent of them were using direct deposit in fiscal year 1987 and the agencies concluded that there is little prospect of increasing their use of direct deposit. Nationwide, there are about 4.5 million recipients of Supplemental Security Income benefits. We were told that about 40 percent of them were aged, 2 percent were blind, and 58 percent were disabled.

The project will involve up to 1,000 participants, each of whom will be given a plastic card that can be used to withdraw benefits without charge. Major objectives of the test include (1) improving the level of service to clients without banking accounts and (2) streamlining the process of delivering payments to reduce the associated high costs of administering benefit payments using a paper-based system.

State and Local Actions

Several state and local governments have attempted to resolve the check-cashing difficulties that senior citizens and public assistance recipients may experience. These actions, summarized in the following sections, include negotiating with commercial banks to cash nondepositors' government checks, mandating that banks provide low-cost accounts, and delivering checks to check-cashing centers. Some states regulate check-cashing at check-cashing centers, as is discussed in chapter 2. In some instances, the recipients bear the cost, while in others banks or government agencies bear the cost.

Initiatives are also under way involving the electronic disbursement of benefits through the use of plastic cards. In some instances, recipients do not need to have banking accounts. These programs involve the use of automated teller machines and point-of-sale terminals in retail stores and other locations. Government interest in such technology has increased rapidly and, where implemented, the programs have met with considerable acceptance by both recipients and administrators. The government has borne the delivery costs in these programs.

Ramsey County, Minnesota, Delivers Welfare Benefits Electronically

Ramsey County, Minnesota, began a pilot electronic benefit transfer system project in July 1987 to distribute public assistance cash benefits to about 1,000 participants. The project was initiated because the county was unable to make satisfactory arrangements with local commercial banks to cash welfare recipients' checks free of charge. It did not require recipients to visit or be affiliated with a banking institution. Recipients were able to access their benefits using plastic cards at automatic teller machines and point-of-sale machines, which were operator assisted. These were conveniently located in commercial establishments in the area where the recipients lived, according to a county evaluation of the program. On the basis of the success of the pilot project, the county began expanding the program to almost all Aid to Families with Dependent Children and General Assistance beneficiaries in June 1988.

Ramsey County officials said that the training of each recipient took about an hour. Nearly all of the participants in the pilot project, some of whom could not read or speak English, indicated they had been adequately trained to use the equipment. Non-English speaking participants reportedly did not have a higher rate of problems than English-speaking participants.

The county evaluation of the pilot program reported that 88 percent of all pilot project participants preferred the electronic benefit system to receipt of their checks in the mail. It also said the advantages to recipients included no waiting for the mail or for the bank or check-cashing facility to open, no check cashing fee, convenient locations and longer hours, and greater flexibility because benefits could be withdrawn all at one time or in smaller amounts in several visits to the money machine. The report said the automated system was potentially more secure than a paper-based system, and a county official told us he believes it will reduce fraud and be able to support several different benefit programs. For example, we were told the county planned to implement a pilot program to distribute Food Stamp Program benefits using the automated system. The report concluded that the electronic benefit transfer system worked exceptionally well and was a cost-effective and highly functional alternative that should be implemented countywide to disperse public assistance benefits.

An Ohio County Reduces Banking Institutions' Concerns Over Fraud

In Summit County, Ohio, certain banks agreed with the county government in 1983 to cash welfare checks[7] for nondepositors free of charge. The programs involved include Aid to Families with Dependent Children and General Assistance. The agreement was an outcome of picketing by welfare recipients of several banks that had refused to cash welfare checks for nondepositors. County and banking officials attribute its success to their cooperative efforts in overcoming bank concerns about fraud and educating welfare recipients about the procedures.

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[7] The state and Summit County issue their own payments, called "warrants," which are drawn on the state or county. Under the provision of the Ohio Uniform Commercial Code, a check is a negotiable instrument drawn on a bank. For purposes of simplicity, however, this report includes Ohio warrants under the generic term "check."

As a result of the 1983 agreement, banks agreed to cash welfare checks for nondepositors if the recipients were registered with the bank and provided their photo welfare cards as identification. The county agreed to give the bank branch designated by each benefit recipient a copy of his or her identification card plus a signature card. The county also agreed to indemnify the bank from forgery if it followed proper identification procedures. While banks were not prohibited from charging a fee for cashing the checks, bank officials said they did not. There were few problems, according to the responsible county and banking officials. The agreement was revised in 1987, and the county no longer provides copies of the recipients' welfare and signature cards to the banks, and does not provide indemnification from forgery. Recipients may now cash their checks in any branch of a participating bank. Banking officials told us in early 1988 that since the agreement began in 1983, only one participating bank has reported a loss from cashing Aid to Families with Dependent Children checks; none had reported losses due to cashing General Assistance checks. The county Treasurer said that as of early 1988, the county had not indemnified the banks on any claims.

The Universal Commercial Code and Contractual Agreements to Cash Government Checks

The Uniform Commercial Code requires any bank to honor or dishonor any check drawn on it when presented over the counter for payment, regardless of whether or not the presenter has an account.[8] This is relevant to the government check-cashing issues because state and local governments maintain accounts at banks that are used, among other purposes, to make public assistance payments.

During our work, we also learned that some governmental units have taken steps to alleviate check-cashing problems by contracting with banks that serve as depositories for their funds (both public assistance and otherwise) to cash checks issued by specified local government units free of charge. In New Jersey, certain county and municipal governments contract with depository banks to cash local welfare checks, whether the check is drawn on the depository bank or not. According to a New Jersey official, most of the large New Jersey counties require depository banks to cash at least the Aid to Families with Dependent Children checks. The District of Columbia requires banks holding district funds to cash all district checks. Seven banks in the District of Columbia are depositories of local government funds, and the payees can cash their checks at any of these banks' main offices or branches with proper identification.

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[8] The bank may take appropriate steps to ensure that the check is authentic and the presenter is the payee. The bank has time to make a reasonable examination of the check to determine if it should be honored and paid, usually by checking the balance in the drawer's account.

Rhode Island Banks Have Voluntarily Agreed to Cash Nondepositors' Government Checks

In 1984, members of the Rhode Island Bankers Association, which consists of all of the major commercial banks in Rhode Island, voluntarily agreed to cash nonaccount holders' Aid to Families with Dependent Children checks free of charge. Although the agreement was informal, unwritten, and only applies to these checks, officials from the State Department of Human Services and the Bankers Association told us they believe that most of the commercial banks in the state also cash other welfare and Social Security checks for nondepositors free of charge. The state official believes that Rhode Island's few savings and loan institutions and some credit unions are also willing to cash these checks. He said banks usually require nonaccount holders who are welfare recipients to show their welfare identification cards and at least one other form of identification. (The most commonly accepted forms are from the Department of Transportation and the Department of Elderly Affairs.) An official from the Department of Human Services told us most recipients cash their checks at the same bank where they pick up their food stamp coupons. Thus, the banks have the security of knowing these individuals.[a]

Massachusetts Requires Banks to Cash Resident Pensioner or Retiree Checks Free of Charge

In 1983, Massachusetts enacted legislation requiring every bank doing business in the state to cash federal, state, and local pension, Social Security, and Supplemental Security Income checks free of charge. A limit of $2,500 per check was added in 1985. The legislation does not contain indemnification provisions. In order to get their checks cashed, pensioners and retirees must first register with a banking institution. All branches and main offices provide registration forms. Applicants may have to pay a maximum of $5.00 in order to register. According to a banking official, pensioners and retirees rarely take advantage of this legislative provision because they prefer to take advantage of other state legislation that requires banking institutions to provide free checking and savings accounts to individuals under the age of 18 or over the age of 65.

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[a] Banking institutions play a role in distributing food stamps in some but not all states. According to a 1986 Department of Agriculture report, some banking institutions in 20 states and the District of Columbia provide food stamp services.

Connecticut Requires Banks to Cash State Public Assistance Checks

In 1987, Connecticut passed legislation requiring banks to cash state public assistance checks. The legislation applies to all state-chartered and national banks; savings and loans; and, in certain instances, credit unions. A state official said that regulations implementing this legislation are expected in late 1988. The checks covered include those for Aid to Families with Dependent Children, General Assistance, and Refugee Assistance. To cash a check, the payee must present the banking institution with two acceptable forms of identification, one of which may be supplied by and paid for by the Department of Income Maintenance. Together, these must contain the payee's signature, photograph, and identification number. The department will indemnify a cashing institution's losses if it follows proper procedures. The legislation does not preclude banking institutions from asking the state to reimburse them for cashing nondepositors' public assistance checks.

According to a Department of Income Maintenance official, the legislation was limited to public assistance recipients because they are the poorest of the poor and experience the most check-cashing difficulties. She believes Social Security recipients have fewer problems because they usually have banking accounts and are not as poor as public assistance recipients.

Illinois Delivers Checks Directly to Check Cashers

Illinois' Direct Delivery System is an alternative to sending most Aid to Families with Dependent Children checks, General Assistance checks, food stamps, and medical eligibility cards through the mail. According to a state public official, the Direct Delivery System was adopted in 1975 in Cook County (which includes the City of Chicago) to combat a serious mail theft problem. Since then, the program has been expanded to 25 of the 101 counties in downstate Illinois. (In the 76 counties without the program, check fraud and mail theft are not serious problems.) Private couriers deliver the checks to agents, where the recipients claim them in person. Over 98 percent of the agents participating in this system are check-cashing centers;[10] a few banks and savings and loan institutions participate. The state pays for the courier to deliver the checks but does not compensate the check-cashing centers for handling the checks. However, the centers may charge recipients for cashing their checks at the state-regulated rate, which is 1.2 percent of the face value of the check plus 90 cents. A state public aid official said that the recipients are not required to cash their checks at the place where they receive them, but suspects that a large percentage do.

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[10] In Illinois, check-cashing centers are referred to as currency exchanges and are regulated.

The state government will indemnify direct delivery agents if they follow proper procedures. A public aid official said that his department has provided indemnification for a single check delivered under the Direct Delivery System and that the system is effective against fraud. He said that the number of replacement checks the state writes each month declined from an estimated 12,000 before the direct delivery system was instituted to some 4,000. (The checks being replaced are, for the most part, coming from outlying areas where direct delivery was not implemented.)

Illinois legislation that became effective in 1986 requires financial institutions to provide basic checking accounts for senior citizens. These accounts can be opened with an initial $100 minimum deposit or an agreement to have regularly recurring payments directly deposited into the account. The accounts include 10 free checks per month and do not require a minimum balance. A state regulatory official told us there was not agreement as to whether banks can assess a monthly service fee or other type of maintenance charge for services rendered under the law. No one we spoke with could estimate the number of accounts senior citizens have opened because of the legislation.

New York City Distributes Public Aid Electronically

A spokesman for the New York City Human Resources Administration, Department of Income Maintenance, said that New York City distributes up to 10 different kinds of public aid benefits electronically through a program known as the Electronic Payment File System. There are about 400 agents where recipients can access their benefits. Eighty to 90 percent of these agents are check-cashing centers and the remainder are banks. Benefit recipients are given magnetic cards with their photographs, which they insert in special electronic devices at the participating check-cashing centers or banks. The cards access computer records to tell the agents the amount of benefits due.

New York City began the program as a pilot project in 1981 and expanded it between 1984 and 1986 to include all single-party public assistance programs with benefits distributed directly to recipients, such as Aid to Families with Dependent Children, Home Relief, and food stamps. The city lumps cash benefits together when paying a recipient. Approximately 350,000 recipients receive public assistance payments, and 150,000 receive food stamps. The city and the federal government pay the program's administrative costs. The federal government's share varies depending on the amount of federal money in a particular program.

Before implementing the full program in 1984, New York City's Department of Income Maintenance surveyed participants of the 1981 to 1983 pilot project and found that 94 percent of them preferred the new system to the paper check system. (The Department of Income Maintenance has not gathered any such data since the system was fully implemented.) According to a Department of Income Maintenance official, recipients find the program convenient because their checks cannot be stolen, they obtain their public assistance and food stamps at one location on the same day, and they do not have to pay to cash their checks. He said the city saves $2 million per year. Mail theft and fraud problems have been virtually eliminated.

Conclusions and Matters for Congressional Consideration

Nondepositor access to check-cashing services at banking institutions is a difficult, complex, and emotional issue. While consumer advocacy groups and others believe that many low- and moderate-income consumers have difficulty cashing government checks, nationwide statistically valid data on the extent or cause of difficulties are unavailable. In addition, there is no common agreement as to what constitutes "difficulty." Nevertheless, on the basis of the limited available data, we believe those without banking accounts—nondepositors—are most likely to experience problems.

A nonquantifiable number of these nondepositors cash their government checks at check-cashing centers or through third parties, which may charge a fee or require a minimum purchase. We were told that nondepositors cash their checks at check-cashing centers partly because they have more convenient hours and locations than banking institutions.

There are not sufficient data to accurately measure the scope or severity of problems individuals without banking accounts are experiencing cashing government checks. However, it is our impression that banking institutions in rural areas are more likely than those in urban areas to cash nondepositors' checks. Check-cashing center fees vary. The limited data suggest that while some low-cost checking accounts are less expensive than check-cashing centers, such accounts may not be widely available. Only 18 percent of the banking institutions we surveyed offered or planned to offer "no frills" checking accounts to the general public in 1985 and some had features, such as high minimum balances, that made them inappropriate for low-income individuals.

A higher percentage of families who receive General Assistance, Supplemental Security Income, and Aid to Families with Dependent Children benefit checks lack banking accounts than do families that receive other types of government checks. Social Security retirement recipients and other senior citizens who receive government checks may have more convenient and inexpensive check-cashing options than other government benefit recipients. A large majority of banking institutions offer special accounts for senior citizens, and the Social Security Administration is trying to make direct deposit a more simple and convenient way of receiving benefits.

Requiring banking institutions to cash nondepositor checks is not the only way to improve individuals' access to government benefits. Use of electronic funds transfer technology, for example, has been cited as a way to solve check-cashing problems by bringing more government check recipients into the banking system. Its use could also lower government costs and reduce banking institution concerns about check forgeries and long lines in their lobbies. Current technology can also make benefits available through use of plastic cards at automatic teller machines and point-of-sale outlets. This approach could reduce the concerns of those who do not want to have banking accounts. Recipients could also obtain additional benefits, such as the option not to take the full amount in cash at one time. The Office of Technology Assessment has reported that it is inevitable that federally funded assistance programs will ultimately move to some form of electronic delivery system.

Matters for Congress to Consider

We recognize that there are costs associated with the cashing of government checks. If Congress determines that recipients of certain government checks should not bear these costs or should be assured of a low-cost option, it should consider encouraging methods that utilize plastic cards and electronic funds transfer technology.

Congress may also wish to consider requiring the Departments of Agriculture, Health and Human Services, and the Treasury, in consultation with state and local governments and banking and consumer groups, to assess the present delivery methods for all government benefits and to seek to develop coordinated delivery systems that would better meet the needs of recipients as well as reduce governmental delivery costs.

Appendix I

Survey of Income and Program Participation Methodology

The Bureau of Census' Survey of Income and Program Participation (SIPP) provides information on the demographic and economic situation of persons, families, and households in the United States. Specifically, the data base covers such topics as assets and liabilities, income, employment, education, and participation in government programs. The objective of our SIPP analysis was to obtain economic and demographic information on families which did not have banking accounts. We selected this group because representatives from consumer groups and financial institutions told us that nondepositors were the most likely to experience check-cashing difficulties at banking institutions.

SIPP is based on a multistage stratified sample of the civilian, noninstitutional, resident population of the United States. The first survey, called the 1984 panel, consisted of initially interviewing adults in 19,878 households. Attempts were made to reinterview adults in these households, generally at 4-month intervals, over a total of 3 years. Each successive 4-month period is called a wave.

The data used in this report is from wave seven of the 1984 panel. We selected wave seven because it was the most recently available wave containing information on the number of respondents with noninterest bearing checking accounts as well as other banking accounts. During wave seven, the Bureau of the Census interviewed 14,902 households remaining out of the original sample.

A wave consists of the Bureau of the Census interviewing one fourth of the households in the sample each month for a total of 4 months. This 4-month period is called a reference period. For example, when interviewing one group of households in September 1985, the Bureau of the Census collected information on the months May through August. Likewise, when interviewing another group of households in December, the Bureau of the Census collected information on the months August through November. Some of the survey questions pertain to the entire reference period and are asked only once during an interview. Other survey questions pertain to each of the 4 months in the reference period and are asked four times. In cases where the wave seven data pertained to each month rather than to the entire reference period, we analyzed responses for August 1985 because this is the only month that occurs in all of the reference periods in wave seven.

We chose to analyze the number of families without banking accounts, as opposed to individuals or households, for several reasons. First, it is more likely that at least one person in a nondepositor family will have to cash a check than a single nondepositor individual. Second, members of families in which at least one family member has an account may have better access to banking services than do nondepositor families. Third, family data provided the most accurate estimate of the number of nondepositors receiving government checks. This is because some of the SIPP data elements list two or more family members as receiving one government benefit; for example, a husband and wife receiving joint Social Security benefits.

Prior to analyzing nondepositor families, the structure of the SIPP data base necessitated that we delete all individuals who were not asked if they had banking accounts. The number of families we used for our analysis was 15,522, which, through weighting, enabled us to project to 92.9 million families.

Part of our analysis involved examining the types of government benefits families with and without bank accounts receive. (See app. II for a list of these benefits.) We also analyzed the number of families who receive Treasury checks and the number receiving state and/or local checks. (See figs. 3 and 4 in ch. 3.)

Treasury checks included

- Social Security benefits;
- Supplemental Security Income;
- Veteran's Administration compensation, pensions, and educational assistance; and
- federal civil service, military, and railroad pensions.

State and local checks included

- Aid to Families with Dependent Children,
- foster child care payments,
- General Assistance,
- state unemployment compensation,
- state and local government pensions, and
- Job Training Partnership Allowance.

Some of the government benefits contained in SIPP were excluded from our analysis of Treasury, state, and local checks because (1) they do not normally involve a recipient receiving a check or (2) they are part of a SIPP data field that contains both Treasury and state benefits.

Appendix II

Number and Percent of Nondepositor Families in the United States That Receive Government Payments (1985)

Number columns in thousands

Government Programs	Families participating in government programs		Families in government programs without banking accounts	
	Percent	Number	Percent	Number
Aid to Families with Dependent Children	3%	2,791	75%	2,084
General Assistance	1	798	74	587
Food stamps	6	5,916	73	4,294
School breakfast	2	1,715	65	1,111
Medicaid	8	7,342	60	4,432
Women and Infant Care (WIC)	1	1,384	56	782
School lunch	6	5,915	54	3,216
Public housing	2	2,137	52	1,107
Rental assistance supplemental	2	1,477	51	750
Supplemental Security Income (SSI)	2	2,205	50	1,106
Energy assistance	1	744	47[b]	347[b]
Education programs[c]	2	1,867	19[b]	364[b]
Misc. programs[d]	2	2,205	19	416
Medicare	24	22,125	15	3,219
Social Security	26	23,887	14	3,395
Pensions[e]	8	7,770	8	597

Note:All of the figures in this table have a standard error of less than plus or minus 1 percent.

[a] Based on a projected population of 92.9 million families.

[b] May not be statistically significant.

[c] Education assistance consists of National Direct Student Loans, Supplemental Education Opportunity Grant, Basic Educational Opportunity Grant, Job Training Partnership Act-training Allowance, and GI Bill and other VA educational assistance.

[d] Misc. programs consist of State Unemployment Compensation; Foster Care Child payments; National Guard Reserve pay; State SSI; Black Lung payments; State Temporary Sickness or Disability; Cuban, Indian, or Refugee Assistance; National Guard or Reserve Retirement pay; and all welfare programs not listed in the table.

[e] Pensions consist of federal, state, or local government pensions; military retirement pensions; railroad retirement pensions; and Veterans Administration pensions or compensation.

Source:Bureau of Census' Survey of Income and Program Participation 1985 data as analyzed by GAO.

Appendix III

Treasury Payments (FY 1987)

Table III.1: Treasury Checks Issued
(FY 1987)

	Volume of checks (millions)	Percent of total volume	Dollar value (billions)
Total	**558.9[a]**	**100%[a]**	**$623.9**
Selected categories			
Social Security	248.9	45	$109.2
Supplemental Security Income	45.5	8	11.0
Civil Service benefits	10.4	2	7.8
Veterans Administration benefits	37.4	7	8.2
Railroad Retirement Board benefits	7.2	1	3.7
Federal salaries	14.8	3	[b]
Tax refunds	81.2	15	99.0
Other	113.4	20	385.0

Note: "Treasury checks" as used in this table include those disbursed by the Department of the Treasury itself and those disbursed under authorization from Treasury by other agencies. The latter are included in the "other" category in this table and include Department of Defense and Postal Service checks, among others. Treasury checks do not include those issued by entities acting as fiscal agents for the United States, such as those issued by the Federal Reserve Banks for interest payment on the public debt.

[a] Total does not add due to rounding.

[b] Information included in "other" category.

Source: The basic categories and the volume data were obtained from Treasury officials and reports, primarily the Cumulative Analysis of Work Processed (TFS-37A) and the Rough Volume Indicators reports. The dollar value data were obtained primarily from the program agencies and supplemented when necessary with Treasury estimates.

Table III.2: Treasury Payments by Electronic Funds Transfer (FY 1987)

Category	Volume of total Treasury payments (millions)	Volume EFT (millions)	Percent sent EFT
Social Security benefits	448.7	199.7	45%
Supplemental Security Income benefits	52.8	7.2	14
Civil Service benefits	24.5	14.1	58
Veterans Administration benefits	54.9	17.5	32
Railroad Retirement Board benefits	12.7	5.5	43
Federal salaries	44.5	29.8	67
Tax refunds	81.2	[a]	[a]
Other	170.1	56.7	33
Total	**889.5**[b]	**330.7**[b]	**37%**

Note: "Treasury payments" by electronic funds transfer as used in this report include those disbursed by the Department of the Treasury itself and those disbursed under authorization from Treasury by other agencies. The latter are included in the "other" category in this table and include Department of Defense and Postal Service electronic payments, among others. Treasury payments do not include those issued by entities acting as fiscal agents for the United States, such as those issued by the Federal Reserve Banks for interest payment on the public debt.

[a] EFT volume was 25,000 representing less than 1 percent.

[b] Totals do not add due to rounding.

Source: We compiled and computed these statistics from data provided by Treasury officials, in particular the officials in Treasury's Financial Management Services, and Treasury reports, primarily the Cumulative Analysis of Work Processed (TFS-37A) and the Rough Volume Indicators reports.

Appendix IV

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